

[7132] TRIAL EXAMINER: How was this affidavit prepared? Did Mr. Lee's attorney prepare it, or an attorney?

THE WITNESS: No, Mr. Lee was submitted the participation similar to the one I have already described. He then, together with Mr. Glidden, who was Secretary and Treasurer of Lee, Higginson, worked out a draft of it. Some time after the draft was worked out I was in Boston and Mr. Lee showed it to me and asked me if it covered the scope that I thought it ought to. I had previously described the scope I would like for him to cover. I did that in connection with [7133] describing the purpose for which we wanted the affidavit. He showed me a draft of the scope. As I recall it I made some suggestions to points which had not been covered, and then he and Glidden, so far as I know, I don't know whether his lawyer participated or not, but I know primarily he and Mr. Glidden, that is my understanding, completed the affidavit in the form in which you now find it.

TRIAL EXAMINER: Was Mr. Glidden an attorney?

THE WITNESS: He was Secretary and Treasurer of Lee, Higginson and Company. I don't know what his training was. Of course, I can't say that either one or both of them didn't discuss it with the lawyers of Lee, Higginson and Company. They didn't do it, however, in my presence.

By MR. HALL:

Q. Of what did your suggestions to Mr. Lee consist?

A. I don't recall. I don't recall the detailed suggestions, but there were several points, as I recall, that are now in the affidavit that Mr. Lee had not included in his original draft.

Q. Do you recall those points? A. No, I do not. I simply read hastily over it when he showed it to me and suggested whatever they were that they be covered. He said he would do it. I don't remember the details of it.

Q. Was Mr. Lee aware of the fact that the lower the [7134] valuation the less assistance his statement would be to you? A. I don't know whether he was or not. If so he drew it as a conclusion. I didn't so advise him.

Q. Wasn't he in a position to draw that conclusion since you had told him the purpose of the statement? A. Yes, I think he very well may have drawn that conclusion.

Q. Why did you use Mr. Fisk's determination of \$50 a share for the preferred stock, Mr. Gunn? A. As I recall it is the only one I had and it didn't appear to me to be unreasonable.

Q. Did you consider Mr. Fisk's \$50 valuation reliable? A. I evidently considered it as reliable as anything I could get. I at least used it.

Q. That necessarily means that you considered it reliable evidence as to the cash value of the preferred stock? A. I considered it the most reliable evidence I had. I don't know whether that is reliable or not. I considered it further than that, as I recall, about the only evidence I had.

Q. Do you think Mr. Fisk was in a better position to value the preferred stock than he was to value the common stock? A. No.

Q. Why didn't you use the \$18 valuation he placed on [7135] the common stock? A. Because I had other evidence as to the value of the common stock and I thought it was appropriate to consider all of the evidence.

Q. In other words, if you had other evidence of the cash value of the preferred stock you might have used that also? A. If I considered it reliable, yes, I would have used it, at least taken it into consideration.

Q. Since you didn't accept the \$18 valuation for the common stock fixed by Fisk because of the existence of other evidence, isn't it reasonable to conclude that had you had other evidence it would have caused you to use a cash value other than \$50 for the preferred stock?

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THE WITNESS: No, I don't think that conclusion would follow, Mr. Hall, for two reasons: First, other evidence might have confirmed Mr. Fisk's opinion. Second, the other evidence may not have been of sufficient value to justify varying from the Fisk estimate.

[7136] By Mr. HALL:

Q. The other evidence you had on the common didn't confirm Fisk's valuation. Isn't that so? A. Within a reasonable range I wouldn't say it was too bad as a confirmation.

Q. Isn't it a fact that the \$18 per share as to the common is derived by Mr. Fisk only after giving effect to the \$50 per share for the preferred stock? A. Yes, sir.

Q. Doesn't that of necessity require you to accept the \$18 for the common stock since you used the \$50 for the preferred stock? A. No, sir, it obviously doesn't because the \$50 for the preferred stock was the only evidence I had of the preferred stock value, and I had other evidence than the Fisk \$18 figure for the common stock.

TRIAL EXAMINER: What figures do you divide to get your \$18 from Mr. Fisk's affidavit?

MR. HALL: May I have the Examiner's question, please?

(Examiner's question read.)

MR. KING: Page 79.

THE WITNESS: \$305,000 shown on paragraph 11, page 79 of Exhibit 27 was divided, I believe, by 17,000-some-odd shares to give the \$18 per share.

[7137] By Mr. HALL:

Q. Was it divided by the 17,537 and a half shares shown on Page 53 of Exhibit 26, Mr. Gunn? A. I believe it was, although I have not computed it exactly. I can if you wish.

Q. Will you do that? A. \$305,000 divided by 17,537 appears to be about 17-and-a-half dollars a share, and I believe that was simply rounded off to \$18 a share.

MR. KING: May we have that read?

(Answer read.)

By MR. HALL:

Q. Mr. Gunn, isn't it a fact that by using \$50 per share of the preferred stock, which is based upon a valuation of Fisk's services, you have attributed a value to all the preferred stock based upon a valuation of services, despite the fact that the balance of the preferred stock so valued was not issued for services? A. May I have that question, please?

(Question read.)

THE WITNESS: It is awfully complicated, but I think the answer is no. We have, it is true, arrived at the \$50 per share, rather Mr. Fisk did, through a valuation of his services. That is the one evidence we have, and it is the only means which occurred to me of valuing the preferred [7138] stock. Then the value having been established in that transaction it is quite true it could be assumed that the entire issue of that particular stock had the same value. It is also true that the other stock, the remainder of the issue, was not issued for the same sort of services, at least, that Harvey Fisk and Sons rendered.

By MR. HALL:

Q. Since you are valuing services rather than stock it can not be assumed that all of the stock has the same cash value. Isn't that so? A. No, I don't see how you can make that assumption. I don't see how you can assume that the particular 1,875 shares that Fisk received had a value different from the remainder of the shares of the same issue in the same company that other people received. It seems to me an assumption to that effect would be irrational.

MR. HALL: May I have that answer, please?

(Answer read.)

By MR. HALL:

Q. Those determinations by Mr. Fisk were made some 33 years after the transaction. Right? A. Yes, sir.

Q. And they were made at your request? A. Yes, and my request was made necessary by the theory of original cost.

[7139] Q. And when Mr. Fisk made them he knew you wanted them to support your original cost claim. Isn't that so? A. I think I most assuredly explained the necessity for my coming to him at that late date and bothering him with a thing like this.

. . .

[7140] By MR. HALL:

Q. As a matter of fact, Mr. Gunn, by using \$25 a share for the common stock you are placing a greater value on the services alleged to have been rendered by the Fisk firm than did Mr. Fisk himself. Isn't that so? A. Yes, I believe that is the result. It was necessary for me to arrive at a value for the common stock, and since several people had stated the value differently, my selecting a single value implied a different computed amount of dollars for all the services of those people who did [7141] not conclude that the stock was worth \$25 a share.

In the case of some it made the services more and in the case of others it made the services less.

Q. What did Mr. Fisk value his services at? \$400,000, wasn't it? A. Yes, \$400,000 total.

Q. What have you included for those same services? In other words, what have you valued those services at? A. I valued them at \$532,187.

Q. By using the \$25 valuation for the common stock whose valuation did you lower, Mr. Gunn? A. I think it could be said that I lowered Hutchinson's, perhaps, and I lowered Hopkins. I believe that is all.

Q. Is there any valuation included in your original cost for Hopkins services? A. Not directly. Hopkins serv-

ices were services to Hutchinson, and they were paid for, as I see it, by Hutchinson. That is the reason I must say they are not directly in there. They are in there indirectly.

Q. But they are not included in your original cost claims as Hopkins' services? A. No.

Q. Or Lorenzo Semple? A. Yes, I think they are included in the original cost claim in the amount which was paid to Hutchinson, because [7142] Lorenzo Semple's compensation was one of the obligations that Hutchinson was required to meet out of his part of the cash and stock which he received in exchange for the properties. They are not identified as such, if that is your question.

Q. How can you say that you lowered Hutchinson's determination when he used a valuation range from \$20 to \$30? A. Well, to the extent he had \$30 in his range it was lowered. It was that to which I referred.

Q. To the extent he had \$20 in that range you raised it? A. Yes, sir.

. . .

[7144] Q. Did Penn Water pay Mr. Cole for his services in connection with Mr. Fisk's affidavit? A. Yes, sir, I believe they did.

Q. Did Penn Water reimburse Mr. Fisk for his services? A. Mr. Pliny Fisk, Jr., was paid for his services. I don't recall whether there was any payment to Mr. Pliny Fisk, Sr., or not.

Q. Was anybody else in the Fisk family reimbursed for their services in connection with obtaining Mr. Fisk's statement? A. I am pretty sure they weren't. There was nobody else who assisted him, assisted in the investigation which led up to Mr. Fisk's affidavit.

Q. Since Mr. Fisk states in his affidavit that his recollection of the transactions were dim, are we to understand that you are responsible for refreshing it? A. No, sir. You are to understand it was refreshed by [7145] such information as I furnished to his lawyer and by Mr. Cole.

Q. Do you know whether Mr. Fisk had any independent recollection of the McCall Ferry activity upon which he was able to draw? A. Yes, sir, I know that he did. In the very first conversation I had with him he recalled a great many facts.

Q. What cash value did he recall, Mr. Gunn? A. I didn't discuss any cash value with him the first time I saw him. He recalled the fact that Barnum was, aside from himself, the partner who had the largest interest in the Fisk firm, and he recalled, I believe, that he and Bertron were what he described as joint accounts in the underwriting, and he recalled that the underwriting had been brought to him in a condition of failure, and he recalled many other more or less minor things that I don't remember offhand.

Q. How many conferences did you have with Mr. Fisk after you obtained his statement? A. After I obtained his statement?

Q. Yes. A. I didn't have any. I had only one or two conferences with Mr. Fisk at all, and that was when he was first approached. When I first approached Mr. Fisk I had one discussion of several hours, and I may have had another, although I am not sure. After that Mr. Pliny Fisk, Sr. told me I would have to take up the matter with his counsel, who [7146] was a Mr. Wilton D. Cole, and who was general counsel for Union Bag and Paper Company, I believe, and in any event his offices were in the Woolworth Building. I never saw Mr. Pliny Fisk, Sr. again after the time he gave me those instructions.

Q. In view of the fact that Mr. Fisk admits that he took very little active interest in the management or supervision of McCall Ferry, how was he in a position 33 years after the event to determine the value of the common stock and preferred stock? A. I don't know, but it didn't seem to me his statement that he didn't actually do the managing of the firm but turned it over to Barnum, it didn't seem to me that that statement supports the con-

clusion he knew nothing about it, because as I recall it somewhere in his statement he says it was a custom of their firm to have weekly meetings of the partners and discuss all of the firm's activities, at least once a week.

Q. Would you say that a determination of cash value or expression of opinion as to cash value made contemporaneously with a transaction would be relevant to the determination of cash value?

THE WITNESS: May I have that question?

(Question read.)

THE WITNESS: Do you mean by that, Mr. Hall, that a [7147] determination of cash value or an expression of opinion, or are you using one the same as the other in that question?

By MR. HALL:

Q. Either. A. Well, I would say that a valid determination of a cash value made contemporaneously should be given very considerable weight. An expression of opinion would depend upon the circumstances or any other indication of the value would depend upon the circumstances under which it was made, the purpose for which it was made, and all the things which might enter into it.

Q. In other words, you would want to consider all of them and decide what weight should be attached to them?

A. Yes, I should think so; certainly.

Q. Did you ask Mr. Fisk if he had made any previous valuation of either the McCall common or preferred stock?

A. No, I don't recall that I did because, as I said, I saw Mr. Fisk only once or twice, and the discussions at that time were not devoted to the valuation of the stock but rather to my ascertaining just precisely what had happened in the financing of this firm and what part his firm took.

Q. Didn't you think that a previous valuation of the McCall stock made by Fisk would be pertinent to your determination of the cash value of that stock? [7148]

A. Yes, if the previous valuation were an attempt to determine the cash value I would think it would be pertinent. If it was made for some other purpose it might or might not be pertinent.

Q. But as I understand it, you did not make any inquiry as to whether or not he had made a previous determination? A. No, I never had discussed any stock value with Mr. Fisk previously. However, I do know that in his investigation which he had Mr. Cole make he made an extensive effort to find the records of his firm in which Mr. Cole thought, at least, there might be evidence of what they thought the cash value was.

Q. Those efforts by Mr. Cole to locate the records were of no avail. Is that right? A. They were substantially unsuccessful except for some few pieces, I think, they found at the Pliny Fisk library.

Q. So far as you know Mr. Fisk never attempted to value the McCall common or preferred stock until you made your request for a valuation of the stock in connection with your original cost determination. Is that right? A. That is correct.

Q. Did Mr. Fisk know of any valuations of the McCall common or preferred stock made by his firm or anyone else? A. I don't know. I didn't ask him. I certainly assumed [7149] that if Mr. Fisk did know of any he took them into consideration in expressing his opinion as to the value at a later date.

Q. Then, so far as you know, Mr. Fisk had no knowledge of any contemporary valuation of the McCall common or preferred stock made during the years 1905 to 1907? A. So far as I know he didn't.

Q. Did Mr. Fisk have any records showing actual purchases or sale of McCall common or preferred stock at the time he made his affidavit? A. None that I know of. I am sure if he had any I would have been able to obtain it.

Q. Did Mr. Fisk place a valuation on the risks assumed and the sacrifices made by the bond subscribers?

A. I think you could say that indirectly he did, at least. I don't think he was requested to make a separate determination of it.

Q. What risks assumed and what sacrifices made, did Mr. Fisk consider? A. I assume he considered them all.

Q. What were they? A. I don't know. I can't enumerate them all any more than we previously discussed them.

Q. You don't know whether Mr. Fisk knew of any, either, or thought of any. Is that right? [7150] A. It seems to me that he certainly did. As a matter of fact, he must have weighed those pretty carefully before he undertook to get the bond subscriptions.

Q. Did Mr. Fisk ever discuss with you the risk assumed and the sacrifices made by the bond subscribers? A. No, not with me personally.

Q. Did Mr. Fisk inform you that his stock valuations included an amount for the risk assumed and the sacrifices made by the bond subscriber? A. No, Mr. Fisk didn't inform me of anything other than what you see in Part 9 in Exhibit 27, and discussions that I gained from Mr. Cole as a result of his conferences with Fisk. But I don't remember there was any discussion of such a valuation except as it took place indirectly through Fisk's knowledge of the risks and his consideration of them in his valuation of the securities.

Q. Then you cannot tell us what amount, if any, Fisk included to cover the risk assumed and the sacrifices made by the bond subscribers? A. No, I can't tell you what amount he allotted to that item.

Q. And you cannot state as a fact that Fisk even considered risk assumed and sacrifices made by the bond subscribers in arriving at his valuation of the McCall Ferry securities? [7151] A. I can only draw that as a deduction. I cannot state it as a positive fact. I don't know what Mr. Fisk's precise mental processes were.

Q. Did Mr. Fisk make a study of the security market conditions as they existed in the spring of 1905 in connec-

tion with his valuation of the McCall stock? Can you say that he did? A. I believe he did. I believe it was done by Mr. Cole and by Mr. Pliny Fisk, Jr.

Q. I wasn't referring to either one of those. I am referring only to Mr. Fisk himself. A. Well, I was attempting to explain I believe they gathered some information on that for him.

Q. What information? A. I don't know what would be the scope of it.

Q. What was Mr. Cole's qualification as a financial analyst? A. Well, Mr. Cole was a lawyer, and it is my understanding that he had been connected with a considerable amount of financing.

Q. What, for instance? What do you mean when you refer to a considerable amount of financing? A. Well, financing in connection with Union Bag and Paper Company, and I believe that he was at one time or another counsel in several underwritings.

[7152] Q. Which ones? A. I don't know. I can ask Mr. Cole what his qualifications are if you wish, but I don't know offhand.

Q. Were any of them hydroelectric projects? A. Union Bag and Paper Company has a lot of hydroelectric projects.

Q. When were they financed? A. Oh, in various years. I don't recall now.

Q. Which were financed in 1905? A. I don't know whether or not any of them were. There may have been some but I just don't know. In any event I don't think Mr. Cole would have been counsel on them in 1905 because I don't think he was big enough.

Q. By "big enough," you mean old enough? A. That is what I mean. In other words, he is about as old as you and I, and we weren't doing anything.

Q. Did you ask Mr. Fisk if he had made a study of the security market conditions as they existed in the spring of 1905 in connection with his valuation of the McCall

stock? A. No, sir, I did not. / I did not talk to Mr. Fisk after he arrived at his conclusion as to that.

[7153] Q. Did you ask Mr. Cole? A. It seems to me that during the several months that Mr. Cole was attempting to find records and was discussing this matter off and on with Mr. Fisk that he did mention information concerning the market had been given to Mr. Fisk. However, that is simply a recollection.

Q. What cash value had Mr. Cole decided upon? A. I don't know. I don't know whether he decided upon any or not. It is my understanding Mr. Fisk made the decision as to the cash value.

Q. Mr. Gunn, I am a little confused. I think you have stated at page 430 of the transcript you saw Mr. Pliny Fisk, Sr., two or three times? A. That is my recollection.

Q. What is the fact? Did you see Mr. Pliny Fisk, Sr., two or three times or just once? A. My recollection is that I saw him twice, that I did see him two or three times. However, I note that Mr. Fisk states in one of these documents that he saw me only once. Mr. Fisk made this statement at the conclusion of his investigation into the valuation of stock and his recollection is probably more creditable than mine because I am attempting to remember how many times I saw him eight years ago, and I was seeing a large number of people at that time. It can be said that perhaps my recollection is not as good as was Mr. Fisk's at the time he made the statement.

[7154] Q. When you refer to Mr. Fisk's statement you are referring to the statement made at the bottom of page 70 of Exhibit 27. Is that right? A. Yes, sir.

Q. Mr. Fisk there states among other things that you came to see him in June of 1938 and at that time, "I told Mr. Gunn that I would be very glad to have my son, Pliny Fisk, Jr., and my personal attorney, W. D. Cole, make a search for these records. That was the only occasion upon which I spoke to Mr. Gunn." A. Yes, that is right. I

recall distinctly at that time there was a discussion of several hours I had with Mr. Fisk. When I testified at page 430 that I had seen him two or three times I then thought that I remembered I had seen him on one or two occasions after that, but perhaps my recollection was defective.

Q. Did Mr. Fisk show you any previous valuation of the services of the Fisk firm to McCall Ferry? A. No, sir.

Q. Did you ask Mr. Fisk if he was aware of any previous valuation of his firm's services to the McCall Ferry? A. No, sir. On the occasion I talked with Mr. Fisk, we didn't discuss valuation of either services or stock.

Q. Then so far as you know there never was a previous valuation of services of the Fisk firm? [7155] A. That is right.

[7158] By MR. HALL:

Q. Mr. Gunn, when Mr. Fisk states in his affidavit that his firm arranged for the sale of approximately \$8,000,000 principal amount of bonds, and the preferred stock, he has forgotten, has he not, that \$2,620,000 of the subscriptions were obtained by Lee, Higginson and Company? A. Where do you find that statement, Mr. Hall, on page 72?

Q. Yes, near the top of the second answer? A. May I have the question, please?

(Question read.)

THE WITNESS: No, I don't think he has forgotten, Mr. Hall. He doesn't say his firm sold \$8,000,000 of bonds. It says they simply arranged for the sale of it. Now, as I understood it, his firm did arrange to retain the Lee, Higginson subscription, and it is to that that he is referring there.

By MR. HALL:

Q. The fact is that Lee, Higginson Company did obtain subscriptions to \$2,620,000 principal amount of bonds.

Right? A. Yes, some such amount as that as I recall it.

Q. And the fact is that the Coffin interests obtained bond subscriptions in the principal amount of \$1,550,000. Is that right? [7159] A. I don't know what you mean by "Coffin interests."

Q. I thought we had discussed Coffin interests in the record to some extent already. A. We have, if it is that discussion to which you refer. Then it is my understanding that Coffin and some other people that might be imputed to association with him had raised certain bond subscriptions. I don't remember just what they were.

Q. And adding the \$2,620,000 plus the \$1,550,000 principal amount to which I referred, we arrive at a total of \$4,170,000? A. Yes, sir, those two figures add up to that amount.

Q. And subtracting the \$4,170,000 figure from the total of \$8,075,000 principal amount procured leaves \$3,905,000? A. Yes, sir, roughly \$4,000,000.

Q. That means that the Fisk firm participated in the procuring of a part of the bond subscriptions represented by the figure of \$3,905,000? A. Will you read that, please?

(Question read.)

THE WITNESS: Yes, it means they did what you stated in that question, and also they arranged to retain all of the other subscriptions that had previously been gotten by Lee, Higginson and others.

[7160] By MR. HALL:

Q. And if Bertron, Storrs & Griscom obtained any subscriptions the subscriptions they obtained came out of the amount of \$3,905,000 principal amount? A. I don't recall the facts well enough to say whether or not that is true. As I recall, from the records we examined and which are included in Exhibit 27 of Bertron, it was impossible to actually trace who had obtained what particular subscriptions.

Q. If Bertron, Storrs & Griscom sold any subscriptions they necessarily had to sell part of the \$3,905,000 amount that I referred to? A. Well, no. I don't think that follows. It might have been a part of what has been ascribed, the Bertron subscriptions may have been a part of those subscriptions which have been assigned to Coffin.

Q. But you don't know that is a fact? A. No, I don't know either way. It is impossible to trace who obtained what subscriptions.

[7167] By MR. HALL:

Q. The earliest valuation appearing in the records of Bertron, Storrs and Griscom is November 21, 1906, more than a year after the date the stock was issued by McCall Ferry. Isn't that so? A. Yes, sir, that appears to be correct.

Q. Construction had not begun at the time of the transaction but was well under way in November of 1906. Isn't that so? That is the transaction which resulted in the issuance of the stock? A. I believe that is correct. I can check it if you wish.

Q. Yes, will you check it? Didn't construction begin in October, 1905? [7168] A. Yes, as I understand, it did.

Q. The dates of completion of the project and realization of earnings were a year nearer in November of 1906. Isn't that right? A. Yes, sir, I think that is correct.

Q. Wouldn't you—— A. At least they thought it was. Let's put it that way.

Q. At that time they thought it was? A. Yes, that is right.

Q. And we must consider these records only prospectively? A. I think that is correct.

Q. In the sense in which they were making them? A. Yes, I believe that is correct.

Q. Wouldn't you expect the stock, if it in fact had a value, to be worth more in 1906 than in the spring of 1905?

A. Yes, I would think it would be worth more.

Q. But even at the date of November, 1906, Bertron, Storrs and Griscom placed a book value of only \$1.00 a share on the common stock and \$10 a share on the preferred stock. Isn't that so?

THE WITNESS: May I have that question, please?

(Question read.)

THE WITNESS: They recorded those two stocks at the values you mention in their books. I don't consider they represent a valuation of the stock.

[7169] Q. The changes Bertron, Storrs and Griscom later made in these valuations were obviously an effort to anticipate the approaching completion of the project. Isn't that so? A. I don't know whether or not they were. It is not obvious to me.

Q. They could have been? A. I don't know.

Q. Bertron, Storrs and Griscom never sold any shares at those valuations or any valuation. Isn't that right? A. Not so far as I know.

. . .

[7170] By MR. HALL:

Q. Isn't it a fact, Mr. Gunn, that as the project approached completion of construction the values reflected on the books of Bertron, Storrs and Griscom increased? A. Yes, I believe up to a certain point they did increase, and then they decreased.

Q. The changes reflected on the records of Bertron, Storrs and Griscom for the common stock are reflected on page 48 of Exhibit 26. Is that right? A. Yes, sir, they are. I might mention in that connection, Mr. Hall, that because of the peculiarity of the change it was largely those facts stated there which caused me to consider that the entries on Bertron's books weren't worth very much as evidence of cash value.

Q. To what peculiarity do you refer? A. Well, on November 21, 1906 they recorded \$1.00. On December 11th, they doubled it and called it \$2.00. On December 31,

they raised it from \$2.00 to \$10.00. Certainly there was nothing in construction during that period of time, nor the nearness to completion, which would have justified any such gyrations as that in the value of stock, or at least nothing I can imagine.

Q. Do you consider an \$8.00 increase between November 21, 1906 and December 31, 1906, a gyration in the stock? A. It certainly is in my language when it lies between [7171] \$2.00 and \$10.

Q. Is that increase an unjustified gyration?

THE WITNESS: I don't know. It is just a gyration.

By MR. HALL:

Q. Did you consider that it was an unjustified increase? A. No, I just considered I didn't know what it was for, and because of those gyrations I referred to I didn't think any of them were worth very much as evidence of the value of the stock.

Q. Do you have a record of the values placed on the books of Bertron, Storrs and Griscom for the preferred stock? A. Yes, sir, I believe that is given on page 47 of Exhibit-28. It seems to have been similarly gyrating, except one of them was left out. If you will notice on November 21 they had it at \$10. a share and on December 31, which was about four or five weeks later, they raised it to \$40 a share. Next April they raised it to \$50. I just [7172] don't know what they were doing to those valuations. They don't look like valid valuations to me, though.

Q. When did the McCall Ferry financial difficulties begin? Just before December 31, 1907, right? A. Yes, in the latter part of 1907 they began to realize they were in difficulty.

Q. And on December 28, 1908, what was the situation financially?

THE WITNESS: May I have the question, please?

(Question read.)

THE WITNESS: McCall Ferry Power Company had defaulted on its bond interest.

By MR. HALL:

Q. Mr. Gunn, the only shares that Bertron, Storrs and Griscom ever purchased were the 150 shares of common stock they had promised to Pullen in 1905 in connection with the acquisition of Pullen's option. Isn't that so?

MR. KING: May I have that question, please?

(Question read).

THE WITNESS: That is all I know of.

TRIAL EXAMINER: 1905 or 1907?

MR. HALL: They had promised to Pullen in 1905, Mr. Examiner. The purchase was made in 1907 by Bertron, Storrs and Griscom.

THE WITNESS: May I have the question and answer again, [7173] please?

(Question and answer read.)

THE WITNESS: Yes, that is the only purchase I know of.

By MR. HALL:

Q. Was that a cash purchase? A. I don't know whether or not it was. I presume it was.

Q. Will you refer to page 190 of Exhibit 27? Is that page from a cash book? A. It appears to be.

Q. And since the Pullen purchase appears there we may draw the reasonable inference that cash was paid?

A. Yes, I think you may.

Q. That purchase by Bertron, Storrs and Griscom was made on August 9, 1907, when the plant was nearing completion. Is that right? A. That is correct. It was also made at a time when Bertron had stated in his account a ten dollar value for stock. It seems to me that he bought an imaginary bargain.

Q. That purchase was made over two years later than the date of issuance of the stock. Isn't that so? A. Yes, sir.

Q. In the summer of 1907 the officers were making rather confident predictions of selling power by June, 1908. Is that right? [7174] A. June, 1908?

Q. Yes. A. I don't recall whether or not that is a fact. Perhaps I can verify it if you wish.

. . .

[7178] By MR. HALL:

Q. The Bertron, Storrs & Griscom records were the only contemporaneous records, is that right? A. The only contemporaneous records but there is no possible way for us to know whether Bertron had some sort of an arrangement with Pullen whereby he had agreed to take that stock from them at \$5 a share at the time the Pullen option was secured. I am not saying he did do it, but I am saying that very well may have accounted for it.

Q. Do you think that Bertron, Storrs & Griscom were [7179] fulfilling an obligation to Pullen? A. I think they might have been.

Q. And that obligation was being fulfilled by Bertron, Storrs & Griscom at \$5 a share. Is that right? A. It was being fulfilled at \$5 a share and for that reason I do not think it could be construed to represent a sale establishing value at all.

. . .

[7206] By MR. HALL:

Q. Mr. Gunn, will you refer to page 8 of Exhibit 27? A. Yes, sir, I have it before me.

Q. Doesn't it there appear that the value of 20 to 30 dollars per share referred to by Mr. Hutchinson was determined by earnings alone?

THE WITNESS: May I have the question, please?

(Question read.)

THE WITNESS: He says his conclusion was based upon earnings alone. Those are the precise words.

By MR. HALL:

Q. You have no reason to doubt that? **A.** No.

Q. Hutchinson does not say in his affidavit that that value could have been secured from a willing buyer at the time of the transaction for cash. Isn't that so? **A.** He does not say he could. He does not say he couldn't. He just doesn't say.

Q. And isn't it a fact that the twenty to thirty dollars per share valuation used by Mr. Hutchinson could have had reference only to earnings in the future? **A.** I don't know whether that would be true or not. That very well may have been Mr. Hutchinson's manner of expressing it. Mr. Hutchinson had been asked to state what he thought [7207] the value was at the time the securities were received by him and I take that statement to mean he thought they were worth from 20 to 30 dollars a share.

Q. In terms of earnings alone? **A.** He has those words in there. I don't know what they mean. I think if you are going to take any implication out of those words it might be that if other things were considered he thought the stock had a greater value.

[7208] **MR. GOLDBERG:** Questions have been asked to elicit from the witness what use he made of these affidavits and what there is in them to support the use he made of them. These people are not here. They are not made available for cross-examination. We have no means of knowing what weight or how the exhibits are to be approached except the exhibit itself and some attempt to find out from the only man we have made available to us who had anything to do with the preparation of these exhibits, or who has had contact with the individuals involved, what in the world these vague and indefinite statements in the affidavits mean.

Personally we are of the opinion they are worthless.

TRIAL EXAMINER: Very well.
Proceed.

MR. KING: If your Honor please, I move to strike the last phrase "We are of the opinion they are worthless." It contributes nothing to the record and is proper comment, if proper at all, in the brief.

TRIAL EXAMINER: Motion to strike is denied.

[7209] By MR. HALL:

Q. In view of the fact that the valuation of 20 to 30 dollars was to be as of a date prior to the realization of earnings, the earnings that he has reference to necessarily were prospective earnings. Isn't that so?

MR. KING: Your Honor, there again it calls for speculation.

TRIAL EXAMINER: He doesn't have to speculate. If he doesn't know he says so. If he does, based upon what other information he may have, he may answer.

MR. KING: The question is not pitched that way. To [7210] answer at all it requires speculation. I object to the question.

TRIAL EXAMINER: Objection overruled.

THE WITNESS: May I have the question, please?

(Question read.)

THE WITNESS: Yes, I think that is right. I think they were prospective earnings of the initial project probably, not the ultimate project.

By MR. HALL:

Q. And that is borne out, Mr. Gunn, by the fact that Mr. Hutchinson based the 20 to 30 dollars on a dividend of from two to three per cent of its par value of the common stock. Is that right?

THE WITNESS: May I have the question, please?

(Question read.)

THE WITNESS: Yes, I would say that is correct. Whether that is all Mr. Hutchinson had in mind in reaching the conclusion I don't know.

[7215] TRIAL EXAMINER: How did he get from two to three per cent return on par value to a valuation of \$20 to \$30 per share?

THE WITNESS: I don't know. That is just what I was trying to explain, Mr. Examiner.

The two to three per cent, as I understood it, relates to the initial project. Then after 1, 2, 3, or maybe 4 years it was contemplated the project would be considerably extended and would very materially increase the earnings from the common stock based upon the initial project alone, and it is the consideration that Hutchinson gave to that of which [7216] I am not aware.

TRIAL EXAMINER: How did he capitalize the two or three per cent returns and get \$20 to \$30?

THE WITNESS: I don't know. I don't know whether he based that on a simple capitalization or not. If you are going to assume that it is a simple capitalization then it would seem to me he capitalized it at about ten per cent.

By MR. HALL?

Q. Mr. Gunn, do you know the persons who fully concurred in the opinion as to the \$20 to \$30 per share valuation used by Mr. Hutchinson? A. No, I do not. Mr. Hutchinson there referred to the people who were associated with the McCall Ferry enterprise, and I don't know which ones he had in mind. I presume he had in mind generally the people who were closely associated with him. It might have been the board of directors, for example.

Q. Did you ask Mr. Hutchinson whom he had in mind?

A. No, I did not. I assume he had in mind people connected with the McCall Ferry Power Company.

Q. Do you know whether Hutchinson investigated the market conditions in 1905 to determine the reasonableness of his conclusions with respect to the cash value of the securities of McCall Ferry? A. May I have that question again, please?

[7217]: (Question read.)

THE WITNESS: I don't know whether he investigated the stock market conditions but he investigated very thoroughly the power market conditions. I assume since he lived during that period he certainly had some knowledge of what the money market conditions were.

By MR. HALL:

Q. What experience did Mr. Hutchinson have in financial matters, if you know? A. I do not know. I know he had been connected with several enterprises, but just precisely the capacity in which he was connected I do not know.

Q. Had Mr. Hutchinson ever made any valuation of stock that you know of? A. No, not except as he would have evaluated stock in buying and selling it for his own use or for whomever he may have bought it.

Q. Had McCall Ferry continued in business on the basis of the original capitalization plus the additional funds needed to complete the project, it would have been a very long time, wouldn't it, before any surplus would have been available as dividends to the common stockholders?

A. I haven't made any computation of that but I assume it would have been a considerable period of years.

Q. Mr. Hutchinson made his valuation solely for your [7218] use in connection with the original cost studies?

A. Well, that was the occasion for my asking him to make it. I presume he made it for any and every use for which it might be needed.

Q. And it was made about 34 years after the event?
A. Some such period of years. The date of the affidavit shows it.

Q. You are claiming a cash value of \$25 for the common and \$50 for the preferred stock in the spring of 1905. Right? A. Yes, sir.

Q. Had any construction been started at that time?
A. No, sir.

Q. The fact is that the plans for the project at that time had not been fully completed. Right? A. That is correct, they had not been fully perfected.

Q. And further the site and location of the dam had not been definitely settled? A. That is right, it had not.

Q. Isn't it also a fact that no construction bids had been called for or received in the spring of 1905? A. Yes, sir.

Q. And it had not been determined who was to construct the project. Isn't that so? A. What is the question, please?

[7219] (Question read.)

THE WITNESS: That is correct, except that McCall Ferry Power Company would. I take it you mean by that question it had not been determined what contractor would construct it. Is that it?

By MR. HALL:

Q. That is right. A. That is right, the contractor had not been selected.

Q. What was the date of the construction contract?
[7220] A. Cooper's contract was dated October 18, 1905. That is shown on page 58 of Exhibit 26.

Q. I believe you have indicated in the spring of 1905 it had not been decided whether McCall Ferry would build a project itself or let someone else do it. Is that right?
A. No. What I was attempting to indicate at that point, what I was attempting to ascertain, was what your question meant.

Q. Yes. A. You simply asked me if it had been decided who would build the project. My answer was that it had been decided that McCall Ferry, as a corporation, would build it or have it built, and that the contractor had not actually been selected.

Q. Was that in the spring of 1905? A. I think we are all tangled up now. In the spring of 1905 it was determined that a project would be built by McCall Ferry Power Company, but the contractor for the actual construction of the project had not then been selected.

Q. And bids were not called for until August. Is that right? A. I believe that is correct.

Q. In other words, in the spring of 1905 the McCall Ferry Company did not know whether they would construct the project themselves or let someone else do it for them?

[7221] MR. SPARKS: ~~May~~ I object to that part of the question, letting someone else do it for them, unless you specify who it means?

MR. HALL: Obtaining a contractor.

THE WITNESS: I don't think McCall Ferry Power Company ever considered constructing the project without obtaining a contractor in one way or the other.

Does that answer your question?

By MR. HALL:

Q. Yes.

The total construction cost of the project had not been determined in the spring of 1905. Isn't that so? A. Well, an estimate had been prepared but it was on a project different in scope from the project actually built, and therefore the ultimate cost was different.

Q. It was not based upon the completed plans at that time either. Is that right? A. What does "It" refer to?

Q. The company had not finally determined what the plans would be? A. No, not in final detail.

Q. Do you think that an estimated dividend rate of two to three per cent fixes any specific value on stock?

THE WITNESS: May I have the question?

(Question read.)

[7222] THE WITNESS: That standing alone, I don't know whether it would or not. However, I think Hutchinson had much more information at his disposal than that figure standing alone.

By MR. HALL:

Q. Will you refer at this time to page 49 of Exhibit 26, Mr. Gunn? A. Page 49?

Q. Of Exhibit 26. You there indicate the prospectus which is part 5 of Exhibit 27, shows estimated earnings equal to seven per cent on the proposed issue of four million dollars par value common stock. Right?

THE WITNESS: May I have the question?

(Question read.)

THE WITNESS: Yes, that is what is there shown. However, the actual issue was five million dollars.

By MR. HALL:

Q. Referring to that estimate and all the other information that you had, you nevertheless stated "An estimated return of seven per cent on the common stock does not fix any specific value on that stock." A. That is my opinion of it. I couldn't fix the value standing on that alone.

Q. And that is the same sort of information Hutchinson was using on page 8 of Exhibit 27. Right? A. Yes, plus all other things he knew about the project. [7223] He used that sort of information plus all other knowledge he had of the project and its development.

. . .

[7311]

GEORGE W. SPAULDING

RE-DIRECT EXAMINATION.

By MR. SPARKS:

[7316] Q. Did Safe Harbor agree to the termination of the contract identified as Exhibit 71 and the exclusion of Safe Harbor as a party to the new contract, Exhibit 72? A. Yes.

[7317] Q. Mr. Spaulding, are these letters which have just been identified as Exhibits 160 and 161 the correspondence between Penn Water and Safe Harbor regarding the termination of the contract identified as Exhibit 71 and the execution of the contract identified as Exhibit 72? A. They are.

[7321] Q. Will you briefly illustrate the process of determining the savings from a single interchange transaction for a single hour? A. I previously stated in my testimony that an interchange transaction really involves three stages. The first a scheduling stage, second, an operating stage, and third, an accounting stage.

In considering the "savings" we are concerned only with the accounting procedure. Suppose, then, that based on a scheduled interchange transaction the load dispatchers have arranged for the supply of interchange energy and capacity from Penn Water and Safe Harbor to one of their Pennsylvania customers. Some time after the actual operations have occurred the customer who received such interchange supply will advise Penn Water of its estimate of the additional operating costs that would have been incurred by them had the interchange supply from Penn Water and Safe Harbor not been received. Such estimated costs will include that customers cost in boiler operations, of starting units, of savings in fuel, and any reduced cost allowance for incremental labor and for maintenance. For

this same period of the interchange transaction, Baltimore Company will similarly estimate their actual increased cost of operation, resulting possibly from the operation of additional boilers or units, their cost of [7322] additional fuel burned, the cost of any additional labor where needed, and any allowance for incremental maintenance, these being costs which they would not have incurred in the absence of this interchange transaction.

Baltimore Company's additional operating costs will, of course, be less than the reduction in operating expenses of Penn Water's and Safe Harbor's customers. Otherwise no interchange transaction would have been scheduled. The difference between Baltimore Company's additional operating costs and the Pennsylvania customer's reduced operating costs is the savings which are divided between the suppliers and their Pennsylvania customer, the receivers.

Q. How is this division of savings accomplished?

A. To accomplish this division of the "savings" and it is usually on a 50-50 basis, Penn Water bills the Pennsylvania customer in connection with this transaction as a part of its interchange bill for that month an amount computed at one-half of the sum of the reduced operating costs of the customer and the increased operating costs incurred by Baltimore Company.

The actual savings on the transaction do not appear on the bills as rendered. Only the billing costs and revenues are recorded in the operating accounts of Penn Water.

TRIAL EXAMINER: May I have the last sentence, please?

(Answer read.)

[7323] By MR. GOLDBERG:

Q. After Penn Water has received the revenues for such interchange—

TRIAL EXAMINER: Just a minute. That part of that answer is not understandable by me. Do you expect the witness to develop it?

MR. SPARKS: I can ask him to do it right now, if your Honor please.

By MR. SPARKS:

Q. Mr. Spaulding, would you explain the last clause in your last answer?

MR. GOLDBERG: Let's have that last clause.

By MR. SPARKS:

Q. Which reads "Only the billing costs and revenues are recorded in the operating accounts of Penn Water"?

A. I am trying to distinguish, Mr. Examiner, between the recording on operating accounts of what was frequently referred to as "savings" on these interchange transactions and the actual billing which is recorded as revenue on the operating accounts of Penn Water.

The revenue so received will, of course, include the actual costs incurred plus an increment equal to one-half of the total savings, and they are the revenues that are recorded on operating accounts and not the savings as was frequently referred to both by myself and by Commission Staff [7324] counsel in that cross-examination.

TRIAL EXAMINER: As I understand it, you do not show in Penn Water's books the incremental cost that would be incurred by the Pennsylvania receiver, nor do you show the incremental costs that will be incurred by Consolidated.

All that your books show would be the revenues that Penn Water receives from the Pennsylvania receiver or customer?

THE WITNESS: May I have that last question?

(Trial Examiner's question read.)

THE WITNESS: That is correct.

TRIAL EXAMINER: The billing costs that you referred to which would be reflected in the books would consist of what?

THE WITNESS: The billing costs, as used here, in contradistinction to revenues, were the payments that Penn Water might make to that customer for a purchase rather than a sale.

MR. GOLDBERG: How about using some figures and letting us see how it works? Take six mills as what it would have cost the Pennsylvania customer, four mills as what it would have cost Consolidated. Then what do you do?

THE WITNESS: You would, as I have explained, add the sum of those two costs together, and divide by two, and would bill the Pennsylvania customer at the rate of five mills per kilowatt hour if energy alone is involved.

MR. GOLDBERG: And then the money involved at the rate of [7325] five mills per kilowatt hour received from the Pennsylvania customer is recorded on Penn Water's books as revenue?

THE WITNESS: That is correct.

Then if during another transaction energy is purchased from the Pennsylvania customer as interchange, then there is a cost incurred by Penn Water which is then set up as an expense, and that is the billing costs that I referred to in contradistinction from the billing revenues. It is not in the same transaction but in another transaction in our assumptions here.

MR. GOLDBERG: I wonder if we could follow through that reverse procedure, that is where Penn Water is purchasing?

Let's assume it costs Baltimore six mills and it costs the Pennsylvania customer four mills. What is the procedure then in a purchase by Penn Water?

THE WITNESS: Again, the cost to Penn Water would be five mills, computed in the same manner if there was a 50-50 split as we have assumed. Penn Water would set

up that five mills as part of its operating expenses, or part of its purchased power, and that would be the end of Penn Water's accounts so far as that transaction is concerned.

MR. GOLDBERG: Thank you very much.

By MR. SPARKS:

Q. Mr. Spaulding, after Penn Water has received the revenues for such interchange services, how does Baltimore Company receive the benefit of the savings from such [7326] transactions? A. Regardless of whether Penn Water, Safe Harbor, or some other system plant actually supplied the electric services that entered into such interchange transaction, and it is usually impossible to determine exactly from which plant the service is supplied, Penn Water will receive additional revenue from interchange as the result of such transaction, and these additional revenues reduce the payment which Consolidated will make under the contracts identified as Items H and I.

Q. Will you refer to Exhibit 18 and explain how the revenues from interchange transactions enter into the computation of those bills? A. Referring to Exhibit 18, the additional revenue received by Penn Water will increase the amounts to be recorded in (e) 5, 6 or 7, as the case may be. The resultant reduction in the payment to Penn Water by Baltimore Company is in turn a reduction in Baltimore Company's own operating expenses. Such reduction in the latter's operating expenses will more than offset the increase in its operating expenses incurred at the time of the interchange transaction, and in such manner Baltimore Company receives the full benefit of all operating savings resulting from interchange transactions between Penn Water, Safe Harbor, and their northern customers.

[7327] Q. Mr. Spaulding, in the discussion of "savings" at pages 2884 to 2899, you were asked about "savings" and "economies" resulting from firm power arrangements and coordinated operations.

Did you have any difficulty in understanding these questions, the answers to which appear at transcript page 2887, line 8, page 2896, line 24, and page 2898, line 1?

A. Yes; I did.

Q. Why? A. I did not understand what "savings" or "economies" were referred to in connection with these firm power contracts.

Q. Are there savings involved in the Pennsylvania firm power contracts? A. Yes, in my opinion there are.

Q. Are there savings involved in the contracts with Baltimore identified in this proceeding as Items E, F, and G, and H and I?

[7328] THE WITNESS: Baltimore Company recently stated that it could not obtain or produce the same services now received from Penn Water and Safe Harbor more economically from any other source. Furthermore, in answering Commission counsel's question it seemed to me that I would have to consider the "value of service" rather than "cost of service", and I have no ready answers at this time relating to value of service.

By MR. SPARKS:

Q. Where were the statements made by Baltimore Company to which you have just referred? [7329] A. They are included in the answer of Consolidated Gas Electric Light and Power Company of Baltimore to the Public Service Commission of Maryland in the matter of the investigation of the rates of Baltimore Company. This answer was executed under oath June 5, 1944, by Mr. Cohn, the then president of Baltimore Company. The proceedings before the Public Service Commission of Maryland were known as Cases 4649 and 4661.

[7336] Q. Mr. Spaulding, several times during your cross-examination you referred to the impossibility of painting kilowatt hours. Do you mean that it is at all times impos-

sible on the interconnected system of Penn Water and Safe Harbor to trace the kilowatt hours from a generating source of such energy to the customers' load centers? A. No, it is not always impossible. For example, where there may be only a single source of energy generation supplying a section of the system load there would be no trouble in tracing the kilowatt hours from the source of generation to that load center.

Q. Does this situation ever exist on the Penn Water-Safe Harbor system? A. Yes, it does on certain sections of this system from time to time.

Q. Will you please give an example? A. Under most operating circumstances we have no difficulty in separating the identity of the 25-cycle electric services, including energy, transmitted from the Holtwood Power Development. For example, the Holtwood frequency changers [7337] connecting the 25-cycle and 60-cycle systems at that plant are very frequently shut down. Under such conditions we can be certain that all of the 25-cycle energy sent out from Holtwood is Penn Water's own generated energy. We can, therefore, trace these kilowatt hours from Holtwood to Baltimore and to Lancaster. The character of these 25-cycle services are so distinctive that we have no trouble in tracing or identifying them.

Q. Can you similarly trace or identify the use made of the 25-cycle single phase energy generation at the Safe Harbor plant? A. Yes, but to a more limited extent, because frequently operating conditions require the conversion of power from 60-cycle three phase to 25-cycle single phase by means of the frequency changer at Safe Harbor.

Furthermore, we cannot always trace the energy on the high tension 25-cycle single phase transmission system to the trolley system of the railroad and identify it as being energy generated at Safe Harbor because of its mixture with the electric services flowing into this section of the transmission system from the other sources of supply at Philadelphia and Washington.

Q. You have referred to the conversion of power from 60-cycles to 25-cycles at Holtwood and at Safe Harbor through frequency changer units. Will you please describe such [7338] conversion? A. The frequency changer units installed at Holtwood and at Safe Harbor consist, for each unit, of two large rotating machines directly connected to a single shaft, each machine being designed to operate from time to time as either a synchronous motor or a synchronous generator, depending upon the operating service requirements.

The machine on one end of the frequency changing unit is designed for operation at 60-cycles and the one at the other end at 25-cycles.

If power is being converted from 60-cycles to 25-cycles, the 60-cycle machine will be operated as a motor, driving the 25-cycle machine as a generator by the mechanical power transmitted through its direct connected shaft, and, similarly, when power is converted from 25-cycle to 60-cycle the 25-cycle machine will be acting as the motor and the 60-cycle machine as the generator.

The direction of power flow, and the amount of conversion, may be controlled at Safe Harbor by mechanically varying the relative position of a stator, thus changing the electrical phase angle.

[7339] Q. Can you normally trace and identify the 60-cycle energy supplied at Holtwood or Safe Harbor to the load centers of Penn Water and Safe Harbor's customers?

A. Not normally, because there is usually a co-mingling of the energy and other electric service attributes generated at Holtwood and at Safe Harbor, and frequently a further co-mingling with backfeed from one of their Pennsylvania customers or from Baltimore.

Q. Does it ever happen that all of the electric services originate at the Baltimore and Washington Steam Plants?

A. No, such operation does not occur.

Q. If all the energy were generated in Baltimore and Washington, would you then be able to trace this energy

to your Pennsylvania customers? A. If at such time we were not receiving any interchange energy over Penn Water and Safe Harbor's interconnections with their Pennsylvania customers, there could be little doubt but that such energy supply would be traceable from its generating source in Baltimore and Washington to Penn Water and Safe Harbor's customers and to the Pennsylvania Railroad through Safe Harbor. Even under such operating circumstances Penn Water and Safe Harbor would be contributing certain essential attributes of the electric service being supplied in Pennsylvania. The energy so supplied by Baltimore to Penn Water and Safe Harbor would necessarily be changed [7340] in voltage and perhaps in frequency, would be mixed with reactive or wattless energy, and would be backed up by the spinning reserve capacity supplied by the hydro units operating as condensers, so that although we might be able to trace the energy from the generating source to the load centers we would find such resulting electric services would be considerably altered in their essential characteristics.

* * *

[7343] By Mr. SPARKS:

Q. Mr. Spaulding, was parallel operation of Metropolitan Edison Company system and Penn Water system continuous from December 6, 1931? A. No. Regular parallel operation was not possible until the end of January, 1932.

Q. Had Penn Water made the necessary changes in its equipment at Holtwood prior to January, 1932?

TRIAL EXAMINER: Will you read that?

(Question read.)

THE WITNESS: Yes, in October, 1931, Penn Water rearranged its transformer units at Holtwood to provide additional capacity for its York circuits. These changes were made coincident with other changes required in its transformers and circuits to provide for the operation of the

tie circuits between the Holtwood and the Safe Harbor plants.

By MR. SPARKS:

Q. When parallel operation with Metropolitan Edison [7344] was established in January, 1932, was the tie circuit between Holtwood and Safe Harbor then in operation?

A. Yes. The Safe Harbor-Holtwood tie circuits went into service a few weeks prior to the parallel operation with Metropolitan Edison.

Q. Then, in January of 1932, both the tie lines from Penn Water to Metropolitan Edison and the tie lines from Holtwood to Safe Harbor were in operation and electric services from Safe Harbor could have been used by Penn Water for supply to Metropolitan Edison? A. That is correct. However, it was recognized that in such operation Safe Harbor might be acting beyond its authority received from the Pennsylvania Public Service Commission, which did not include permission to sell or dispose of Safe Harbor's services directly or indirectly to Metropolitan Edison.

Q. How was this situation corrected? A. The situation was immediately corrected by separating various amounts of Holtwood generating capacity from the rest of the Penn Water system and connecting it only to the York circuits for the supply of electric services to the Edison Light and Power Company and to the Metropolitan Edison Company, under the contracts identified as Exhibits 138 and 139. Such operation, however, was not as economical nor as reliable as would result from this supply being paralleled [7345] with the main power system of Penn Water and Safe Harbor.

Q. How long did this segregated method of operation of the York supply continue? A. About one year. On January 10, 1933, Safe Harbor obtained additional authority, granted by order of the Public Service Commission, permitting it to sell or dispose of its services to Metropolitan Edison Company among others.

Q. Mr. Spaulding, I show you a document entitled "Copy—Application of the Safe Harbor Water Power Corporation for a Certificate of Public Convenience, evidencing the Commission's approval of the modification of the order of the Public Service Commission issued to the Safe Harbor Water Power Corporation on the 31st day of March, A. D. 1930," consisting of an application and a report and order of the Pennsylvania Public Service Commission, and I ask you if that is a true copy of the application and order filed in January of 1933? A. It is.

Q. Mr. Spaulding, does the application show that it was executed on the 29th day of March, 1932? A. It does.

Q. And is the date of filing which I mentioned, of January, 1933, incorrect? I am referring to the filing of the application. A. The application was filed in March of 1932.

[7346] Q. And is the order of the Commission as of January 10, 1933? A. That is correct.

MR. SPARKS: I ask, Mr. Examiner, that this document be marked for identification as Exhibit 163.

TRIAL EXAMINER: The document handed the reporter may be marked Exhibit 163 for Identification.

(The document referred to was marked Exhibit No. 163 for Identification.)

By MR. SPARKS:

Q. Mr. Spaulding, does this document contain the application and order which you identified for the record at transcript pages 3454 and 3455? A. It does.

Q. Will you please indicate the dates on which parallel operation directly between Penn Water or Safe Harbor's generating plants and the main system of Pennsylvania Power and Light Company was begun? A. The hydroelectric plants of Penn Water and Safe Harbor were first paralleled directly with the main system of Pennsylvania Power and Light on October 8, 1935. Such parallel

operation was specifically contemplated under the contract identified as Exhibit 76 and this parallel operation was made possible upon the completion by Pennsylvania Power and Light of its 66 K. V. transmission circuit between its [7347] Harrisburg sub-station and its Donegal sub-station northwest of the city of Lancaster where a connection was made to an existing 66 K. V. circuit extending from Safe Harbor to this Donegal sub-station, a distribution center of Pennsylvania Power and Light Company. These interconnection facilities, including those provided by Penn Water and Safe Harbor at Safe Harbor and Manor sub-station, were used more or less continuously until November 1939 and this interconnection of Penn Water and Safe Harbor with P. P. & L. has been used continuously since that date.

Q. When were the facilities of Penn Water and Safe Harbor first paralleled directly with the Philadelphia Electric Company's main system? A. Parallel operation of Safe Harbor and Penn Water's system with that of the main system of Philadelphia Electric Company resulted from the continuous parallel operation of the Pennsylvania Railroad's extensive transmission system in the manner contemplated under the provisions of the contracts identified as Exhibits 134 and 135.

Such parallel operation of the single phase power supply facilities of Penn Water, Safe Harbor and Philadelphia Electric Company was tested out on October 30, 1934, was operated more or less continuously until June, 1938, and since 1938 all of the railroad's power supply sources, other than that from New York City, have been operated in parallel.

[7348] TRIAL EXAMINER: What do you mean by "Parallel operation"?

THE WITNESS: By parallel operation is meant the operation of two systems, or sources of power supply, in synchronism as a result of an electrical connection between

those two systems, and as a result of that electrical connection those two systems are electrically tied together.

TRIAL EXAMINER: What is the difference between calling it a parallel operation and just saying the systems were connected as of a certain date and remained so over a period of time? d

THE WITNESS: I don't think there is any distinction, as long as the expression "tied together" means electrically tied together.

TRIAL EXAMINER: Is that the full significance of the term as it appears in the contracts insofar as an engineering interpretation of those contracts is concerned?

THE WITNESS: Yes, sir, I think it is, remembering, of course, that when you refer to tying together two systems it may imply tying together parts of two systems, and that is the reason I used the expression "the main system of" because by "main" I meant to include all of the electrical transmission system and the sources of supply available to that particular company and operated together as a system.

TRIAL EXAMINER: Does "parallel operation" connote cooperation of any kind?

[7349] **THE WITNESS:** No, sir. Parallel operation as I use it, and as I know of its use, means only the actual operation.

TRIAL EXAMINER: It doesn't signify in addition power factor cooperation?

THE WITNESS: No, sir, it does not signify that.

Of course there must be that result but it does not signify anything other than just the technical fact you tie two circuits together electrically.

TRIAL EXAMINER: All right, Mr. Sparks.

By MR. SPARKS:

Q. At pages 3615 and 3616 Mr. Goldberg was questioning the justification for your allocation of the entire cost of the two—220 K. V. Safe Harbor-Baltimore-Washington transmission lines to Baltimore Company in Exhibit 35, was he not? A. That is right.

Q. You did assign the entire cost of those lines to Baltimore Company in Exhibit 35, did you not? A. Yes, sir. In my opinion the total cost of those lines should be allocated 100 per cent to Baltimore Company.

Q. Are those transmission lines used at times for backfeed? A. Yes, practically all of the backfeed from Baltimore and Washington to Safe Harbor and Penn Water is transmitted over those lines.

[7350] Q. Do you consider the transmission of such backfeed to Safe Harbor and Penn Water a service that Penn Water renders to Baltimore Company? A. Yes, I do.

Q. Will you briefly state for what general purpose backfeed is supplied from Baltimore and Washington to Safe Harbor and Penn Water over these facilities? A. Generally, the backfeed is so supplied to accomplish the maximum overall economy of system operations. More specifically, such backfeed is supplied by Baltimore Company to Penn Water and Safe Harbor for three different purposes:

First, as electric services supplied to the hydro companies in connection with interchange transactions between these two hydro companies and their northern customers.

Second, as electric services to supplement the power resources of Penn Water and Safe Harbor in meeting their operating responsibilities to their firm power customers, and

Third, for conversion by Safe Harbor and supply to the Pennsylvania Railroad through the facilities of Penn Water and Safe Harbor, because Baltimore Company has

no facilities of its own for the supply of electric services to the Pennsylvania Railroad to meet Baltimore Company's operating responsibilities under the railroad power supply contract, identified as Exhibit 10.

[7351] Q. Considering now these three different purposes for backfeed separately, will you indicate why, in your opinion, any costs relating to, or that might be allocated to such backfeed for interchange transactions, should be considered a cost to Baltimore Company? A. As I have frequently testified, the savings on interchange transactions are equitably divided between Penn Water and the northern customers. All of such savings allocated to Penn Water are ultimately a benefit to Baltimore Company. There are necessarily certain costs incurred in providing for such interchange transactions and the savings or benefits derived go in part to compensate for such costs. When Penn Water or Safe Harbor use backfeed from Baltimore in connection with such transactions, Penn Water and Safe Harbor do not retain any of these benefits or savings, but, because Baltimore Company does receive Penn Water's and Safe Harbor's share of the benefit and savings, Baltimore Company should bear any costs incurred by Penn Water and Safe Harbor in connection with such transactions.

Q. Do the customers in Pennsylvania make any investment or incur costs for facilities for interchange? A. Yes. These customers have themselves provided quite extensive transmission systems of their own which are used in this connection and, in addition, the costs of Penn Water's lines serving them would also be properly considered [7352] a cost to be allocated to such customer. These transmission systems in Pennsylvania are just as essential in such interchange transactions as are the lines from Safe Harbor to Baltimore.

None of the costs of transmission to the north of the hydro plants were allocated to Baltimore and there is no reason why the customers in Pennsylvania should be allo-

cated any of the costs for transmission between the hydro plants and Baltimore.

Q. Now, will you state why, in your opinion, any costs relating to or that might be allocated to such backfeed, used by Penn Water and Safe Harbor to supplement their own electric services rendered to their firm power customers, should be considered a cost to Baltimore Company?

A. The operations of the hydro plants of Penn Water and Safe Harbor are carried out to obtain maximum economy of operations, the benefits of which wholly accrue to Baltimore Company. As one example of such operation, Baltimore Company obtains hydro services at a time when it can replace the highest cost service on Baltimore's own system. To obtain the maximum benefits the hydro companies are operated on the peak of the load curve, as was explained in connection with Exhibit Number 8. With this method of operation, Baltimore Company sends Penn Water and Safe Harbor as backfeed electric services in the off-peak hours when they can [7353] be supplied by Baltimore Company at a minimum cost to itself. Inasmuch as Baltimore Company receives the full benefit from the economies of such operation, it is only proper that Baltimore Company be allocated any costs incurred in connection with the backfeed necessary for the procurement of these economies, and I believe we properly considered that Penn Water was rendering transmission services to Baltimore Company when it transmitted backfeed from Baltimore Company for such purpose.

TRIAL EXAMINER: Would you read that last, please?

(Answer read.)

By MR. SPARKS:

Q. Will you also state why, in your opinion, any costs relating to, or that might be allocated to, such backfeed from Baltimore for conversion by Safe Harbor and supply to the Pennsylvania Railroad through the facilities of Penn

Water and Safe Harbor should be considered a cost to Baltimore Company? A. To the extent that such backfeed supplied to the railroad is the operating responsibility of Baltimore Company, it is again only proper that any transmission costs relating to such backfeed be allocated to Baltimore Company, for a transmission service is thus rendered by Penn Water to Baltimore Company.

Q. Will you briefly state the several reasons why the [7354] entire cost of the Safe Harbor-Baltimore-Washington Lines should be allocated to Baltimore? A. In the first place, considering the part of these circuits between Ellicott Sub-station and the connection with the Washington Company, this line, together with Ellicott Sub-station is clearly provided in connection with Baltimore Company's contract with Potomac Electric Power Company to which Penn^o Water is not a party.

With respect to the circuits between Safe Harbor and Baltimore, there are a number of important uses in addition to that of providing capacity and energy services, and all for Baltimore's use in meeting its own system obligations. The second of the two circuits between Safe Harbor and Baltimore, installed about 1937, was provided for Baltimore Company alone, and only to assure electric stability and reliability of service.

Q. What are these uses other than for capacity and energy services? A. One very important use is in connection with power factor cooperation. To permit Baltimore to operate its modern and efficient steam plants at maximum loads it is necessary that such plants carry near 100 per cent power factor. The hydro plants at Holtwood and Safe Harbor provide the required wattless power, often by operating hydro units as condensers.

Another use is in connection with the maintenance of [7355] satisfactory system frequency. The Baltimore system load, principally because of the Bethlehem Steel Company load, is subject to very heavy and rapid load fluctuations. In the absence of the tie-lines through Safe Harbor

to the north, these load fluctuations would create a serious problem of frequency and load regulation. About 75 per cent of these load fluctuations are carried by these tie-lines and absorbed in the several large inter-connected systems in Pennsylvania and New Jersey. It might be mentioned that the existence of the fluctuating load in the Baltimore system, and the need for carrying a considerable part of these fluctuations on the tie-lines, limits the capacity use of these tie-lines to the north and is a use of these lines by Baltimore Company, not compensated by any similar use by other customers, but for which use no cost was allocated against Baltimore Company.

TRIAL EXAMINER: In what sense do you use "capacity" in connection with those tie-lines?

THE WITNESS: The capacity of a tie-line may be limited by the size of the conductor, or it may be limited by the connected transformers at one end or the other. From a consideration of those two principal factors it can be determined what the maximum load carrying capacity of those tie-lines is.

If, for instance, it would be possible to continuously [7356] carry a steady load of 50,000 kilowatts on a transmission line with its connected transformers, and then for reasons of outside influence the power and energy flowing over those lines were widely fluctuating, perhaps to the extent of 20 or 30,000 kilowatts, then you can see that the continuous rating of those lines may be only half what it was before, because there is an upper limit to what you can carry on those lines, and if you have a widely fluctuating load the integration of the steady load must necessarily be much less than its rating would otherwise be.

Other factors that have to be considered in that is one of stability, one of voltage regulation between the two ends of the line, and one of the relay settings of that line in order that such relay settings may be coordinated with the other safety protection relays on the system.

[7378] Q. In your testimony you have referred to three methods of recording energy. You have referred to gross amounts, to net amounts, and to net hourly amounts. Will you please explain these terms more specifically? A. I will do so by example. If we were to add up the sum of all the energy registered on ratcheted meters, measuring the amount of power flowing toward Baltimore from Holtwood and Safe Harbor for one hour, a day or a year, we would obtain a gross figure.

As I have already stated, such a gross amount is not practical for operating purposes because we know that frequently power may be flowing in two different directions on the same circuit within a single clock hour, and again that power may be flowing north on one of our Baltimore circuits while flowing south on another Baltimore circuit, perhaps even at the same instant.

Nevertheless, gross amounts are recorded and are generally used only in connection with the records shown in Exhibit 143, and in our Commission reports wherever requested.

For most operating purposes we determine and record the net power flow on these several circuits for each hour. The separate totals of the "net hourly" flows in each direction are what we refer to as "net hourly" records.

"Net" records can be obtained either by taking the difference between the gross records or the algebraic sum of the [7379] "net hourly" records. However, we frequently find that the "net" of the north and south gross figures is so small that we get no indication of the large amount of actual energy services rendered in each direction. It is for this reason, in my opinion, that we must consider the "net hourly" figures for any practical analyses or for cost of service purposes, and we have, therefore, used these "net hourly" deliveries and receipts in connection with our analyses of energy transactions in Exhibit 35.

[7381] Q. Is a substantial part of the electric energy generated by Safe Harbor consumed at points in the state of

Pennsylvania? A. Yes. Using the statistics compiled by the company in the manner shown in Exhibit 143 for the years 1944, 1945, and for the first ten months of 1946, and expressing the sum of Item 1 plus Item 15 as a percentage of Item 10, we obtain a maximum percentage of 55 per cent for 1944, 58 per cent for 1945, and 51 per cent for the first ten months of 1946.

Not only is Item 1 greater in amount than should properly be used in any such accurate determination of the energy generated at Safe Harbor and consumed in states other than Pennsylvania, but Item 15 is also greater in amount than should properly be used by reason of the fact that a large but undetermined portion of Item 15 is in part backfeed received from Baltimore, and included in the amount shown [7382] in Item 2 of Exhibit 143, and in part interchange received from Philadelphia Electric Company at Perryville. These above percentages, subject to the inaccuracies stated, show that of the energy generated at Safe Harbor less than 58 per cent is transmitted to states other than Pennsylvania, and therefore the balance, which is a substantial part of such energy generated at Safe Harbor, is consumed in the state of Pennsylvania.

. . .

[7383] Q. Can you conclude from these statistics that Baltimore did not receive two-thirds of Safe Harbor's output, Mr. Spaulding? A. Yes, I can, but it must be understood that such computation of energy proportions, while clearly indicating that Baltimore did not receive two-thirds of the energy generated at Safe Harbor, do not represent nor measure the proportion of the electrical services rendered, nor the proportion of the electrical services supplied by Safe Harbor to Baltimore Company, for electric energy is not a measure of the electric services rendered nor a measure of the services available.

. . .

[7397] Q. Mr. Spaulding, do I understand that Pennsylvania Power and Light Company required supplemental

services to meet the firm power obligations on their own system? A. Yes, they did.

Q. Do these interconnected companies frequently depend on such interchange services to supplement their own power resources in meeting their system requirements?

A: Yes.

. . .

[7402]

J. RHOADS FOSTER.

. . .

[7404]

RE-DIRECT EXAMINATION.

By MR. SPARKS:

Q. Dr. Foster, at page 100 of the transcript, lines 15 and 16, you were asked, "Did you have in mind the use of a credit to consumers in connection with the depreciated rate base?"

You answered "Yes."

Did you misunderstand the question? A. Yes. The answer should have been "No."

Q. At pages 5656 to 5659 of the transcript you illustrated the use of a depreciated and an undepreciated rate base. For this purpose you assumed utility plant accounts in an aggregate amount of \$5,300,000, and made related assumptions.

In this connection have you prepared an exhibit having [7405] the title "Illustrations of different methods of treating depreciation within the rate making formula."? A. I have.

Q. Dr. Foster, I hand you a document entitled "Illustrations of different methods of treating depreciation within the rate making formula," and ask you if that one sheet document is the document to which you have just referred?

A. It is.

Q. Was that document prepared by you or under your supervision? A. It was.

MR. SPARKS: Mr. Examiner, may this document be marked for Identification as Exhibit No. 165?

TRIAL EXAMINER: The document handed the reporter will be so marked.

(Thereupon, the document referred to was marked Exhibit No. 165 for Identification.)

By MR. SPARKS:

Q. Do the hypothetical data appearing on Exhibit 165 show variations of the two methods, namely, use of a depreciated and undepreciated rate base? A. They do.

Q. Is this exhibit the source of the figures which you mentioned at page 5656 of the transcript? A. It is.

[7406] Q. In the first and second lines of the exhibit have you shown the original cost of utility plant and the depreciation reserve balance which you have assumed to exist in a hypothetical situation? A. I have.

Q. What are the assumptions which you have made as to alternative treatments of depreciation in rate regulation? A. Cases 1 and 2 assume the use of an undepreciated rate base. The rate base is assumed to be \$5,300,000, the amount of original investment.

Cases 3 and 4 each assume the use of a depreciated rate base. In case 3 the assumed rate base is \$5,031,000 and in case 4 it is \$4,000,000.

Q. In each case have you assumed that the fair rate of return is 6.5 per cent and that the regulatory authority has allowed this 6.5 per cent as the fair and reasonable rate of return? A. Yes. This rate is shown in line 5 of the exhibit.

Q. Have you shown on line 6 for each case the product of the rate of return times the rate base? A. I have. The product of the rate of return applied to the rate base is \$344,500 in cases 1 and 2, \$327,000 in case 3, and \$299,000 in case 4.

Q. Have you carried to line 14, utility operating income, the amount of this return allowed by the regulatory

authority? [7407] A. I have. The amounts on line 14 are the same as the amounts on line 6.

Q. Have you for the illustrative purposes in cases 1 and 2 included a deduction representing what is assumed to be credits to consumers for the earning capacity of depreciation funds? A. Yes. The credit is shown on line 20 among the income deductions. In case 1 the deduction is at a rate of $2\frac{1}{2}$ per cent, and in case 2 it is at the rate of $6\frac{1}{2}$ per cent on the depreciation reserve balance.

Q. Is the credit to consumers shown on line 20 as \$17,500 in case 1 and \$45,500 in case 2, an operating expense? A. No, it is considered to be compensation for the use of funds other than the capital funds provided by stockholders. Therefore, the amount of the credit must be deducted from income before income is available for payment of dividends.

Q. Is the amount of the credit applied to reduce the annual provision for depreciation which is charged as an operating revenue deduction? A. It is.

Q. So that the operating revenue is correspondingly less than the amount which otherwise would be required to yield the return allowed by the regulatory authority? [7408] A. That is correct.

Q. In connection with the use of a depreciated rate base is there such a credit to consumers? A. No. In cases 3 and 4 there is no deduction on line 20 representing a credit to consumers.

[7409] Q. What have you assumed as the annual provision for depreciation? A. \$106,000.

Q. In cases 3 and 4 does the recognition of depreciation take the form of a deduction from the rate base? A. It does. In case 4 the assumed deduction is an amount equivalent to the depreciation reserve. In case 3 the assumed deduction is five-thirteenths of the depreciation reserve corresponding to the ratio of the credit to the consumers shown in line 20 for case 2.

Q. Is this distinction the reason for your statement at page 704 of the transcript that the "use of a depreci-

ated rate base provides indirectly the credit which is provided directly by the adjustment of the fair return where the mode of treatment is the use of an undepreciated rate base"? A. That is right.

Q. Is the assumed fair rate of return of 6.5 per cent the same in each of the four cases illustrating different methods of regulatory treatment of depreciation in rate making? A. Yes.

Q. Is the effective return, that is the dollars actually available to investors, the same in each of the four cases? [7410] A. No; in cases 1 and 3 it is the same and in cases 2 and 4 it is the same.

Q. Is the effective rate of return which investors would earn on their investment the same in each of the four cases? A. No. In cases 1 and 3 it is the same and in cases 2 and 4 it is the same.

Q. At page 5669 of the transcript, lines 14-16, you said, "The results of the determination which follow from applying the six per cent rate of return to an original cost rate base are consistent with the first test, that of equitableness." Was that a complete statement? A. No. The experienced cost rate of six per cent was determined subject to the definition of experienced cost of capital at page 515, lines 6-11 of the transcript in this proceeding. Therefore, the application of six per cent rate to an original cost rate base is consistent with the test of equitableness only to the extent that the components of that rate represent return on debt and preferred stock capital.

Q. At page 5691 of the transcript, lines 10 to 23, you said that you know of no feasible procedure by which it is possible, "to directly determine the dollars of the fair return requirement so far as equity capital is concerned."

You then said that in this proceeding the certain number of dollars, not less than \$2,450,000, were not determined [7411] before you "turned your attention to the question of fair rate of return."

Do you feel it necessary to clarify those statements?

A. Yes. In the answer at lines 22 and 23 and in the answer

to the preceding question, I had reference to the general question of whether or not the fair annual return to a regulated enterprise, expressed in dollars, may be estimated directly, without consideration of either rate base or rate of return.

The desire for administrative simplicity sometimes has raised the question as to whether or not the fair annual return might be determined directly without the use of either a rate of return or rate base.

I was referring to this general question when I said that I know of no feasible procedure by which it is possible to determine directly the fair return on equity capital. A rate of return or percentage cost must be estimated for equity capital and can be given expression as an annual return only by multiplication of some base.

The amounts of 2,430,000 to 3,150,000, shown by Schedule 11 of Exhibit 30—

MR. GOLDBERG: Just a minute, Dr. Foster. May I refer to those schedules?

Is that the beginning of a long answer about Schedule 11 or is that one sentence you have there?

[7412] MR. SPARKS: About one paragraph, Mr. Goldberg.

THE WITNESS: Three or four sentences.

MR. GOLDBERG: Mr. Examiner, I object to any testimony on Schedule 11 in so far as it relates to II(a) through IV(b).

MR. SPARKS: May I say this, Mr. Examiner: There was reference during the cross-examination to Schedule 11, one, in Dr. Foster's answer to a question of Mr. Goldberg's, and also there was reference in some of Mr. Goldberg's questions to the replacement cost of capital.

In order to clear up this question of the determination of the dollars of fair return and of the rate of return and of the rate base we have to have this oppor-

tunity to state what Dr. Foster did in determining the fair rate of return.

That is a perfectly proper matter on redirect examination.

TRIAL EXAMINER: What Dr. Foster did in determining the fair rate of return, so far as his direct testimony was concerned, counsel stated was based upon a part of that schedule 11 which the Examiner excluded.

MR. SPARKS: That is right.

TRIAL EXAMINER: Are you taking the position that that ruling has to be modified?

MR. SPARKS: No, sir.

Don't let that last statement of mine be any qualification of our position that schedule 11 ought to be in the [7413] record. But at this time all we are doing is relating this redirect testimony to matters involved in the cross-examination.

TRIAL EXAMINER: Can you point to the place in the record where that is referred to?

MR. SPARKS: Yes, sir.

TRIAL EXAMINER: May I have the question and the answer as far as the witness has gone, please?

(Question and answer read.)

MR. SPARKS: Let me point out to Your Honor the figure of \$2,450,000 mentioned in Mr. Goldberg's question at line 19, Page 5691 was taken by Dr. Foster, or derived from Schedule 11.

TRIAL EXAMINER: Let me see the transcript, please.

MR. SPARKS: Yes, sir.

TRIAL EXAMINER: Where else does that amount come from?

MR. GOLDBERG: It is not in the record, Mr. Examiner.

TRIAL EXAMINER: Where were you referring to it?

MR. GOLDBERG: Dr. Foster used that figure, didn't he?

MR. SPARKS: Yes.

TRIAL EXAMINER: On cross-examination?

MR. GOLDBERG: On direct examination.

MR. SPARKS: That is right.

MR. GOLDBERG: That was the amount of dollars, not less than that amount of dollars.

[7414] MR. SPARKS: That is right. That is the amount of fair return.

MR. GOLDBERG: The only cross-examination which related to the excluded part of Exhibit 11 had nothing to do with replacement cost of capital which, incidentally, is not Exhibit 11—

MR. SPARKS: I didn't say it was.

MR. GOLDBERG: The only question which was asked was to the effect "Could you have reached your conclusion in this case without the excluded portions of Schedule 11 of Exhibit 30?" All we wanted to know was what is the basis for his 6.5 answer. We did not go into the question of the use of the excluded portion. That is what they are trying to do now.

Suppose a witness decided that reproduction cost is the only means of determining fair rates, and he came in with testimony on that basis? But the Commission before whom he appears has long ago decided that that is not a competent basis and they won't listen to it?

TRIAL EXAMINER (Interposing): Let me have the answer of the witness where he refers to Schedule 11.

MR. SPARKS: You mean at a prior place in the transcript?

TRIAL EXAMINER: No, right here.

MR. SPARKS: We have not finished the answer, Your Honor.

MR. GOLDBERG: I interposed.

[7415] TRIAL EXAMINER: Let the reporter read what he has.

(The following answer of the witness was read by the reporter:

"A. Yes. In the answer at lines 22 and 23 and in the answer to the preceding question, I had reference to the general question of whether or not the fair annual return to a regulated enterprise, expressed in dollars, may be estimated directly, without consideration of either rate base or rate of return.

"The desire for administrative simplicity sometimes has raised the question as to whether or not the fair annual return might be determined directly without the use of either a rate of return or rate base.

"I was referring to this general question when I said that I know of no feasible procedure by which it is possible to determine directly the fair return on equity capital. A rate of return or percentage cost must be estimated for equity capital and can be given expression as an annual return only by multiplication of some base.

"The amounts of 2,430,000 to 3,160,000, shown by Schedule 11 of Exhibit 30——")

TRIAL EXAMINER: May I have the question now, please?

(The following question asked the witness previous to the above-mentioned answer was read by the reporter:

[7416] "Q. At Page 5691 of the transcript, lines 10 to 23, you said that you know of no feasible procedure by which it is possible, 'to directly determine the dollars of the fair return requirement so far as equity capital is concerned.'

"You then said that in this proceeding the certain number of dollars, not less than \$2,450,000, were not determined before you 'turned your attention to the question of fair rate of return.'

"Do you feel it necessary to clarify those statements?")

TRIAL EXAMINER: When you asked the witness if he thinks it necessary to clarify the statement you are coming right back to the type of question the Examiner criticized this morning.

MR. SPARKS: May I state the purpose of that question, if Your Honor Please?

TRIAL EXAMINER: Yes.

MR. SPARKS: There is the implication, we feel, which should be corrected at this time, or the answer of Dr. Foster should be clarified in order that there may be no implication of inconsistency between what he said at 5691, in answer to Mr. Goldberg's question, and the method which he used in determining his rate of return. That is the purpose of the question and the answer. In the part of the answer which has [7417] not been completed Dr. Foster will attempt to show that the answer to the question which I pointed out to Your Honor on 5691 should have been amplified so as to show exactly what he did there so that there will be no implication left in the record as the result of his answer to Mr. Goldberg's question—

MR. GOLDBERG: Mr. Examiner?

MR. SPARKS: —of inconsistency.

TRIAL EXAMINER: You are asking the Trial Examiner to resign his function of ruling on the relevancy and materiality of questions to the witness.

MR. SPARKS: No, sir. I am only submitting my views to you.

TRIAL EXAMINER: Your question is in such form that the Examiner can only permit the witness to answer by resigning to the witness the function of determining relevancy and materiality.

MR. SPARKS: Mr. Examiner, counsel and the witness for the Respondent have to make the determination for themselves. That, then, is submitted to you for your consideration. If we didn't first make the determination for ourselves we never would have anything to present here.

MR. GOLDBERG: I am entitled to the protection, Mr. Examiner, of a proper question. There wasn't the slightest suggestion that that question would bring forth an answer [7418] bearing on the material to which I have objected and which the Examiner stated he was going to exclude.

MR. SPARKS: Yes.

MR. GOLDBERG: It was only when he started that sentence, that was the first time I had any notice that he was going into objectionable material, and that is the only time when I was able to interrupt and stop him.

TRIAL EXAMINER: The question is whether the witness wishes to clarify his previous answer?

MR. SPARKS: Yes, sir.

TRIAL EXAMINER: The witness has answered yes. Is that not right?

MR. SPARKS: Yes, sir.

TRIAL EXAMINER: Is that the way the answer starts?

MR. SPARKS: Yes. It starts "Yes." Then he proceeds to clarify.

TRIAL EXAMINER: Everything after "Yes" is stricken.

MR. SPARKS: We take an exception, if Your Honor please.

TRIAL EXAMINER: Let it be understood that this ruling is on a parity with the ruling which came up in a similar instance this morning in connection with the re-direct examination of the witness Spaulding. No evidence is being excluded. It is a question of putting proper questions to the witness.

MR. GOLDBERG: At least up to this time no evidence is [7419] being excluded, Mr. Examiner, because I will make an objection to any reference in any answer to those portions of Schedule 11 that I objected to.

TRIAL EXAMINER: All right.

MR. SPARKS: Recognizing the Examiner's ruling without acceding to it:

By MR. SPARKS:

Q. Dr. Foster, will you state in what respects you feel it necessary to clarify those statements to which you have referred at page 5691 of the transcript?

MR. GOLDBERG: I object to the form of the question. The witness ought to be asked first why he thinks any clarification is necessary.

MR. SPARKS: I don't think so. That is foolish, if Your Honor please.

MR. GOLDBERG: Why is it foolish?

MR. SPARKS: Ridiculous.

MR. GOLDBERG: We have heard statements about implications.

TRIAL EXAMINER: Read the question.

(Question read.)

TRIAL EXAMINER: The witness is to observe the import of the Examiner's ruling in giving his answer to this question.

MR. SPARKS: Yes, sir.

[7420] TRIAL EXAMINER: And is not immediately to proceed to give the same answer that he did in response to the previous question.

MR. SPARKS: Well, if Your Honor please, I thought that Mr. Goldberg's objection to the previous answer was only to the last incompleted sentence which Dr. Foster had testified to. He did not object to that portion of the answer preceding the incomplete sentence.

MR. GOLDBERG: Is the witness in his answer going to stop just before the reference to Schedule 11 of Exhibit 30?

MR. SPARKS: I don't think he is.

If Your Honor please, let me say this: If any portion of his answer is objectionable I recognize Your Honor's right and duty to exclude it if it properly should be excluded. But we have a portion of an answer here which was not objected to, and which I think Your Honor would not take objection to, certainly down to the sentence which was incompleted.

TRIAL EXAMINER: Read the question, please.

(The following question was read by the reporter:

"Q. Dr. Foster, will you state in what respects you feel it necessary to clarify those statements to which you have referred at page 5691 of the transcript?")

TRIAL EXAMINER: Having in mind the statements that have been made by counsel for the Respondents, particularly in indicating the witness' going to launch forth into a long [7421] answer, with respect to which this question is a mere type, the Examiner will rule that the witness may not answer the question in its present form. That is made for the same reason and on the same grounds as the previous ruling in connection with striking the previous question.

MR. SPARKS: I take exception to Your Honor's ruling on the basis we are being deprived of the right to a fair hearing by not being permitted to present proper re-direct testimony.

MR. GOLDBERG: Proper re-direct testimony based upon implications of inconsistency?

MR. SPARKS: Based upon cross-examination which counsel for the Commission launched into while this witness was on the stand under cross-examination.

MR. GOLDBERG: Point out where counsel for the staff went into how the witness used that portion of Schedule 11 of Exhibit 30 that he has objected to.

TRIAL EXAMINER: Very well. We will come to that in due course.

You can put a question to the witness which will elicit from the witness whatever he wishes to clarify in regard to cross-examination in an orderly way.

MR. SPARKS: I am not quite clear, if Your Honor please, as to whether the witness' answer in the affirmative to the question as to whether he felt it necessary to clarify those [7422] statements has been left in the record.

TRIAL EXAMINER: It has been.

MR. SPARKS: It has been?

TRIAL EXAMINER: Yes.

MR. SPARKS: Very well, sir.

By MR. SPARKS:

Q. Doctor, in your answer at lines 22 and 23, and in your answer to the preceding question, did you have reference to the general question of whether or not the fair annual return to a regulated enterprise expressed as dollars may be estimated directly without consideration of either rate base or rate of return?

MR. GOLDBERG: Where is this general question that counsel has reference to?

MR. SPARKS: I am asking Dr. Foster——

TRIAL EXAMINER: Let me have the question, please.
(Question read.)

TRIAL EXAMINER: I see no reason why he can't answer that question.

MR. GOLDBERG: I want to be sure, Mr. Examiner, that they are or are not referring to some general question about the subject that I asked during cross-examination. I don't know.

TRIAL EXAMINER: I think if you want to object to the question on specific grounds you may do so. If you want to inquire as to what relation this particular testimony has to [7423] the previous cross I think that comes up under cross properly.

MR. GOLDBERG: I could object to the question, of course, because it is vague and indefinite. But to avoid that I first wanted to ask whether they are referring in that question to some general question I asked on the subject.

MR. SPARKS: We are referring that to your question at page 5691 of the transcript, lines 10 to 23.

MR. GOLDBERG: Let me have that question again, please.

(The following question was read by the reporter:

"Q. Doctor, in your answer at lines 22 and 23,

and in your answer to the preceding question, did you have reference to the general question of whether or not the fair annual return to a regulated enterprise expressed as dollars may be estimated directly without consideration of either rate base or rate of return?").

MR. GOLDBERG: I object, Mr. Examiner. The question was "Do you believe that you must first determine the dollars required for fair return before reaching a conclusion as to fair rate of return?" The answer was "I do not." Anything that came after that had nothing to do with the response to the question I had asked.

TRIAL EXAMINER: Objection is overruled.

MR. SPARKS: May we have the question, please?

(The question was again read by the reporter.)

THE WITNESS: I did.

[7424] By MR. SPARKS:

Q. Doctor, must a rate of return or percentage cost be estimated for equity capital?

[7425] THE WITNESS: In the process of fair return determination I know of no feasible procedure by which the fair return for equity capital can be determined without consideration and use of a percentage rate appropriately reflecting the cost of equity capital to be applied to some base.

[7426] Q. At page 5643, lines 21 to 23 of the transcript, you said that the margin of .869 per cent, subtracted from Penn Water's price ratios for the period since September, 1944, provides the adjusted earnings-price ratios. Is that a correct statement?

MR. GOLDBERG: What line is that?

MR. SPARKS: Lines 21 to 23.

THE WITNESS: No, that statement was in error with respect to the mechanics of the adjustment. The adjustment procedure was correctly described on the following page, 5744, and on page 6023.

The average was determined for the group of six for the period from August 1939 to August 1944, inclusive. It was assumed that during the period from September 1944 to January, 1946, inclusive, the Penn Water earnings-price ratios maintained the same relative position as had previously existed in relation to the average for the group of six. Therefore, the .869 per cent differential was added to the averages for the group of six in order to determine the adjusted earnings-ratios for Penn Water—

MR. GOLDBERG: Did you mean the medial four of six?

[7427] **THE WITNESS:** Added to the average of the medial four of six, yes. Those adjusted earnings-price ratios for Penn Water were used instead of the actual and higher earnings-price ratios in determining the 8.51 per cent.

By MR. SPARKS:

Q. At page 5744 of the transcript a reference was made to a study of a group of 11 earnings-price ratios and to its purpose. What are the facts which determined the availability of the group of six and the group of 11 earnings-price ratios for the purpose of the study? **A.** Prices or quotations were reported for 82 electric or electric-combination operating utility common stocks in the bank and quotation record for January 9, 1946. However, the number of operating utility common stocks traded in the securities markets has been extremely small until recent years because of holding company ownership.

In 1938 the rate and research department of the Federal Communications Commission found only 40 public utility common stocks for which market quotations were available, and some of those were traded so rarely or under such restricted conditions that weight could not reasonably be given to the bid quotations.

The total of 40, moreover, included seven telephone, six manufactured gas, and seven holding company common stocks, leaving only 20 electric and electric-gas operating [7428] company common stocks.

The list of twenty common stocks included those already identified as belonging to the group of eleven. The remaining nine are the common stocks of Pennsylvania Water and Power Company, Philadelphia Electric Company, Southern California Edison Company, Tampa Electric Company, Long Island Lighting Company, two others for which only over-the-counter quotations were available, and the then outstanding issues of three operating companies which were subsequently acquired by or merged into other companies.

In the case of Philadelphia Electric Company the proportion of the outstanding common stock held by United Gas Improvement Company was about 97 per cent prior to disposition during 1943. I excluded the Long Island Lighting common stock because of the non-payment of common dividends and the Tampa stock because of the comparative investor disfavor.

I also had determined the identity of common stocks listed on Securities Exchanges as of January 1, 1946, for which monthly market prices or quotations were available for a long period of years. Ten common stocks are included in this list.

All of the group of six are represented, plus Central Hudson Gas and Electric, Philadelphia Electric, Southern California Edison, and Pennsylvania Water and Power, Hartford Electric, Connecticut Power, Cleveland Electric [7429] Illuminating, and Duke Power were not included.

In this connection I determined for the common stock of each company the volume of trading over the entire period for which prices were available on a securities exchange.

The turnover of the Penn Water common stock had been generally equal to the turnover of the six most actively traded utility common stocks.

Q. At page 5799, lines 8 to 15 of the transcript, you were asked a question based on certain assumptions.

In giving your answer at line 16, did you understand that the question contained the assumption that all participants agree that the regulatory treatment of depreciation, including the use of a depreciated rate base, is fair and reasonable? A. I did.

Q. At page 5819, lines 8 to 14 of the transcript, you said that the increase in the earnings-ratios for the Penn Water common stock from November, 1939, to the end of 1941 was accompanied by similar movements of the earnings-price ratios for other common stocks, and that the movement of the Penn Water earnings-price ratios is not to be explained by the issuance of the license order of November, 1939.

At page 5828, lines 5 to 7 of the transcript, you said that as a general proposition selectivity in the market is greater in times of relative low prices.

[7430] Have you prepared a statement showing the comparative fluctuations of the Penn Water earnings-price ratios and of the earnings-price ratios of certain other common stocks? A. I have.

Q. I show you a one-page document entitled, "Comparative fluctuations of the two lowest and the two highest earnings-price ratios included in the group of 11, together with the Penn Water earnings-price ratios, within phases of cycles," and I ask you whether you can identify that document? A. I can.

Q. Was it prepared by you or under your supervision? A. It was.

MR. SPARKS: May this document as described by the witness be marked exhibit for Identification, No. 166?

TRIAL EXAMINER: It may be marked Exhibit 166 for Identification.

(Thereupon, the document referred to was marked Exhibit No. 166 for Identification.)

By MR. SPARKS:

Q. Will you please describe this exhibit, Doctor? A. The months in which the greatest variations exist among the earnings-price ratios are June 1932, March 1938, and April 1942. I have identified the two common stocks among the group of eleven which had the lowest earnings-price ratios for these three months and the two which had the highest [7431] earnings-price ratios for these three months.

The two common stocks appraised most favorably were those of Hartford Electric and Connecticut Power. The two appraised least favorably were Consolidated Edison and Pacific Gas and Electric.

For these two extremes within the group of 11 and for Penn Water I have shown the average earnings-price ratios at the end of each phase of each cycle. Those terminal months are the months identified on Exhibit 166. Thus prices were high and earnings-price ratios were at their lowest level in August 1929.

Prices were low and earnings-price ratios were at their highest level in June of 1932.

The alternate low and high positions were reached in August of 1936, March 1938, July 1939, April 1942, and January 1946.

I then determined the increase or decrease of the earnings-price ratios from the previous high or low position. Thus in July of 1939, the average for the two lowest earnings-price ratios, those for Hartford Electric and Connecticut Power, was 4.98 per cent.

In April 1942, the average for the same two earnings-price ratios was 7.79 per cent, an increase of 2.81. The increase of 2.81 was an increase of 56 per cent from the level of 4.98 per cent.

[7432] Q. Had you finished your answer to that question, Doctor? A. Yes.

Q. At page 5830, lines 14 to 19 of the transcript, you said that the earnings-price ratios of common stocks appraised by investors as having a greater degree of risk

tend to fluctuate more widely than the earnings-price ratios of common stocks appraised as having a lesser degree of risk.

Do the data shown in Exhibit 166 illustrate the behavior to which you refer? A. Yes. The Hartford Electric and Connecticut Power common stocks on the average have been purchased on a lower yield basis than any other among the eleven.

The Consolidated Edison and Pacific Gas and Electric common stocks on the average have been purchased on a higher yield basis than any other among the 11.

The changes in the earnings-price ratios from one phase to another of a cycle have been greater for the latter two common stocks, in amount and relatively, than in the case of Hartford Electric and Connecticut Power.

Q. How do the fluctuations of the Penn Water earnings-price ratios compare with those of the Hartford Electric and Connecticut Power earnings-price ratios? A. The Penn Water earnings-price ratios were higher during periods of relatively high prices and much higher during [7433] periods of relatively low market prices.

Q. How did the Penn Water earnings-price ratios compare with those of Consolidated Edison and Pacific Gas and Electric? A. The Penn Water earnings-price ratios were higher for August 1929 and for June 1932. They were lower for August 1936, March 1938, July 1939, and April 1942, and higher for January 1946.

The change in comparative position between April 1942 and January 1946 may be explained by the pendency of the rate proceeding.

Q. Did the fluctuations of the Penn Water earnings-price ratios within the intervals between the months shown in Exhibit 166 correspond more closely to the fluctuations characteristic of the two lowest earnings-price ratios or the two highest earnings-price ratios in the group of 11?

A. The two highest.

Q. What was the increase in the Penn Water earnings-price ratio from November 1939 to April 1942? A. From 7.10 to 11.94 per cent, or 4.84.

Q. What was the increase in the average for Consolidated Edison and Pacific Gas and Electric during the same period? A. From 7.96 per cent to 14.26 per cent, or 6.30.

Q. What are these increases expressed as percentages [7434] of the earnings-price ratios for November 1939? A. Sixty-eight per cent for the Penn Water earnings-price ratios and 79 per cent for the average of the earnings-price ratios of the Consolidated Edison and Pacific Gas and Electric common stocks.

Q. What is your conclusion from these data? A. The increase in the Penn Water earnings-price ratios from July 1939 or November 1939 to December 1941, or to April 1942, conformed to the behavior which would be expected if considered in the light of the fluctuations of the earnings-price ratios of other common stocks.

No evidence is available to support a conclusion that the increase in the Penn Water earnings-price ratios during this period was accounted for by the license proceeding.

Q. If the order of November 3, 1939, directing the company to file with the Federal Power Commission an application for a license had an adverse effect on investors appraisals of the Penn Water common stock, would you expect that influence to be evident in the earnings-price ratios of the period immediately following the date of the order? A. I would. However, examination of schedules 1 and 3 of Exhibit 29 shows that from October 1939 to January 1940, the Penn Water earnings-price ratio increased from 7.18 to 7.26, and that the average for the group of six other common stocks, the mean of the medial four, decreased from 7.01 to [7435] 6.94. These movements in opposite directions are each of the magnitude of about one per cent. If the comparative behavior is in fact

accounted for by the license order a composite reappraisal resulting in readjustment to the extent of 1/50th of the previous appraisal in October can scarcely be described as significant.

Q. Doctor, does your answer at page 5857, lines 14 and 15 of the transcript, to the question asked by Mr. Goldberg which appears on the same page at lines 2 to 9, inclusive, require clarification? A. Yes.

MR. GOLDBERG: What is the answer?

(Answer read.)

THE WITNESS: I should have added that such a fact would not necessarily be evidence that the Commission's proceeding challenging the right of Penn Water to maintain a project without a license had a significant effect on Penn Water's earnings-price ratios.

By MR. SPARKS:

Q. At page 4900, lines 11 to 13 of the transcript, Mr. Goldberg asked this question:

"Isn't it really a fact that the cycle you used began in June 1936 rather than August 1939, or August or September 1936?"

At lines 20 to 24 on the same page you characterized the [7436] movement, "From about August of 1936 to August of 1939, as being distinct and appropriately identified as a movement or fluctuation independent of, and not significantly related to, the movements reflected in the behavior at the later dates."

What were your reasons for that statement? A. It is reasonable to conclude that the cycle of earnings-price ratio movement from about September 1936 to about August 1939, was related to general business cycle conditions. The Federal Reserve Board index of industrial production moved upward from a low of 91 in February of 1936 to a high of 123 per cent in May of 1937.

The United States Bureau of Labor Statistics index of wholesale prices also moved gradually upward from

78.6 in May of 1936 to a maximum of 88 per cent in April of 1937.

The market prices of utility common stocks and the movement toward lower earnings-price ratios anticipated this level of increased production and higher commodity prices by some months.

Thereafter the index of industrial production fell with some rapidity from 123 per cent in May of 1937 to a low of 81 per cent in May of 1938.

The index of wholesale commodity prices also fell from 88 in April of 1937 to 78.7 per cent in April of 1938.

The decline in the stock market during the months of [7437] September, October and November 1937, can only be described as a collapse.

Barron's 50-stocks average moved from 136 in January of 1937 to 78 in December of that year.

The decline in market prices of utility common stocks and the corresponding rise in earnings-price ratios shown by Chart 1 of Exhibit 29 probably were closely related to the general business conditions and the loss of business confidence.

The rise of market prices and the decline of the earnings-price ratios during the latter part of 1938 and the first part of 1939 probably was related to the recovery from the depression of 1938.

Q. Were the fluctuations of the earnings-price ratios during the cycle extending from about September 1939 to about January 1946, the apparent result of different causes? A. Yes. The fluctuations during this period scarcely could have been the result of variations of industrial production. The Federal Reserve index of industrial production, which was at 107 per cent in August of 1939, rose steadily until it reached a maximum of 249 in October 1943, and was maintained at nearly that level until May of 1945.

Two special influences were present which did not exist in the period September 1936 to August 1939. The

first was the war and the second was more significant tax changes.

[7438] The stock market was influenced by adverse military needs and, after the swing to offensive operations, the growth of confidence in an early termination of the war.

Another influence on earnings-price ratios was the increase in Federal income tax rates from 19 per cent in 1939 to the high income and excess/profits tax rates established by the Revenue Act of 1942, and the tax reduction which became effective at the beginning of 1946.

Diverse influences were present during the period September 1939 to January 1946. High and low extremes of business confidence were present and had an offsetting influence on the earnings-price ratios. I believe that the average offers a satisfactory representation.

Q. Doctor, at page 5924, lines 16 to 20 of the transcript, Mr. Goldberg asked whether the earnings-price ratios for the period beginning February 1946 appeared to be following the trend of the earnings-price ratios of the cycle which began August 1936 and ended September 1939.

You said that may be true as far as the shape of the curve is concerned, and at page 5925, lines 7 to 9 of the transcript, you said that the behavior during the recent period is largely the result of tax influences. Will you explain those statements? A. The earnings-price ratios is merely a ratio between past earnings as reported or as adjusted and the current market [7439] prices. In preparation of the earnings-price ratios shown by Chart 1 of Exhibit 29, and the earnings-price ratios for the month of January to the month of September 1946, which were read into the report at page 5742, no adjustments were made for the effect of tax changes which were anticipated during 1945 and became effective January 1, 1946.

The prospect of tax reductions resulted in reappraisals of the shares being traded. The market prices reflected the anticipated increases in net income as a result of the

tax change, particularly elimination of the excess profits tax.

The earnings-price ratios which determined the shape of the curve for the first months of 1946 are heavily weighted by 1945 earnings determined without adjustment for the prospective tax change.

The anticipated tax reductions and corresponding increases in net income are in considerable part reflected in the interim statements for the 12 months ended June or July of 1946.

The average market price of the six common stocks continued to rise during the first six months of 1946. The highest market price level was reached in June.

Nevertheless, when based on reported earnings which reflect in increasing degree the realization of the effect of the tax reductions, the earnings-price ratios moved upward beginning in February.

[7440] In January of 1946 the earnings-price ratios were below the true capitalization rate and the upward movement experienced during the first months of 1946 was in the nature of at least a partial corrective so far as the influence of the tax revision is concerned.

Q. At page 6007, lines 9 to 13, of the transcript, in making a distinction between rate of return and return on common stock capital represented in the rate base, you said, "In the case of a utility with only common stock equity there is no difference as a result of that distinction."

Is that a correct statement? A. No. In the case of a utility with only common stock capital the distinction between return and rate of return is, of course, significant. I intended merely to indicate that if there is only common stock capital in the capitalization the distinction is not complicated by the leverage resulting from representation of other kinds of capital in the capitalization.

Q. At page 6024, lines 19 to 25, and at page 6024, lines 1 to 16 of the transcript, the Examiner suggested that the revised earnings-price ratios for the period September 1944

to December 1945, inclusive, be supplied for the record. Have you prepared a schedule showing these revisions?

A. I have.

Q. I show you, Doctor, a one-page document entitled [7441] "Changes in earnings-price ratios for the Penn Water common stock and for the medial four of six common stocks to reflect earnings data becoming available after the preparation of Exhibit 29."

Was that document prepared under your supervision?

A. It was.

MR. SPARKS: May that document be marked Exhibit No. 167 for identification, Mr. Examiner?

TRIAL EXAMINER: Yes, the reporter will mark the document Exhibit 167 for identification.

(Thereupon the document referred to was marked Exhibit No. 167 for Identification).

By MR. SPARKS:

Q. Doctor, at page 6040 of the transcript, lines 22 to 25, Mr. Goldberg asked the following question:

"May I put briefly in the record the distinction I think you are making? You are saying that accounting costs are not economic costs, and those economic costs are the only ones you recognize as costs. Right?"

You answered in the affirmative.

Was that a complete answer? A. No, it was a response to the first part of the question.

[7442] MR. GOLDBERG: Just one moment, please.

I object to the question as not in accordance with the evidence and I move to strike the answer. The question was "You answered in the affirmative. Was that a complete statement?" or words to that effect.

The fact is that he agreed to the statement in the question and said "With the addition of one further point."

In other words, it was not merely an answer in the affirmative and stopping there. He went on to give all the reasons he thought necessary.

MR. SPARKS: No, he didn't, if your Honor please. That is just the purpose now of this further redirect.

MR. GOLDBERG: Who was restraining this witness?

TRIAL EXAMINER: Read the question, please.

(Question read).

TRIAL EXAMINER: May I have the answer too, please?

(Answer read).

MR. SPARKS: He has not completed this answer, Mr. Examiner.

TRIAL EXAMINER: I will sustain the motion to strike. We cannot stop and try now whether those answers were complete or not. He is entitled to answer the question correctly if it was answered incorrectly before.

MR. SPARKS: If your Honor please, this situation springs from the fact there were two questions in that question. Doctor [7443] Foster answered the first part of the question, namely, that accounting costs are not economic costs. He did not on cross-examination answer the second part of the question.

TRIAL EXAMINER: The form in which your question is put is properly objectionable.

MR. SPARKS: I don't understand why, if your Honor please. I have asked him if it was a complete answer. He said "No" in response to the first part of the question.

TRIAL EXAMINER: I do not think we can let the witness determine whether his answer was complete as of the time he gave it or not.

MR. SPARKS: Well, if your Honor please, I think the witness certainly must have some say as to whether he was completely answering the question. He said he did not completely answer it. I say he did not completely answer it.

I submit to your Honor that we ought to have an opportunity to complete the answer to that question. That seems to me to be the purpose of redirect examination.

TRIAL EXAMINER: Procedurally his answer was complete in that he was not interrupted.

MR. SPARKS: Will your Honor indulge just a moment?

MR. GOLDBERG: He went on to say he had one additional point to make. He made it.

MR. SPARKS: Obviously the answer was only to the first part of the question.

[7444] TRIAL EXAMINER: Objection is sustained and the motion to strike is granted.

MR. SPARKS: I take an exception.

By MR. SPARKS:

Q. Doctor, in your studies of the rate of return determination in this case have you disregarded accounted-for costs? A. I have not.

Q. Doctor, were schedules 4 and 5 of Exhibit 29 designed to show anything other than the actual experienced costs of debt and preferred stock capital and the costs as recorded in the accounts of Penn Water as at the time when incurred? A. They were not designed to show anything other than the costs which you have described.

Q. Are debt discount an expense and call premiums costs of supplying service?

MR. GOLDBERG: What does "service" mean?

MR. SPARKS: Service supplied by Penn Water.

MR. GOLDBERG: What service?

MR. SPARKS: Now, if your Honor please,—

TRIAL EXAMINER: Proceed with the witness.

MR. GOLDBERG: Mr. Examiner, you know, you speak of servicing debt, and this is financial cost we are talking about, as I understand it. We have heard the word "service" used in connection with the furnishing and selling of [7445] electric energy.

I am just trying to find out what these things mean.

TRIAL EXAMINER: Do you have any objection to stating whether it applied to debt service or not?

MR. SPARKS: It applies to services rendered by Pennsylvania Water and Power Company.

TRIAL EXAMINER: To its customers.

MR. SPARKS: To its customers.

TRIAL EXAMINER: All right.

THE WITNESS: I believe that at the time when incurred their status as costs is not questionable. An outstanding issue of bonds cannot be redeemed and onerous requirements of an existing debt contract—

MR. GOLDBERG: I move to strike the answer as given up to this point as unresponsive to the question.

TRIAL EXAMINER: Read the question, please.

(Question read.)

[7446] TRIAL EXAMINER: The answer, too, please.

(Answer read.)

MR. SPARKS: That is not a complete answer.

MR. GOLDBERG: I realize that. The reason I interrupted is because it was obvious it would not be responsive.

TRIAL EXAMINER: Finish the sentence.

THE WITNESS: —avoided without the payment of call premium.

TRIAL EXAMINER: Anything more to that answer?

MR. SPARKS: Yes, there is more. It is all responsive. I think Your Honor will recognize it.

TRIAL EXAMINER: Yes, but he gets right back to the same problem which has come up before in connection with permitting the witness to give lengthy answers in response to questions where really the first sentence the witness gives is an answer to the question.

MR. GOLDBERG: If you can call that an answer.

TRIAL EXAMINER: The question is usually in the form of something which requires a simple answer "Yes," and then the witness proceeds from there on on his own.

MR. SPARKS: To qualify and explain that categorical answer. It is perfectly proper.

TRIAL EXAMINER: It gives no one an opportunity to object. The question is retired with the first few words and then the witness is free.

[7447] Your answer to that question is "Yes," is it not?

THE WITNESS: Well,—

TRIAL EXAMINER: Isn't that a complete answer?

THE WITNESS: The question as put to me may be answered "Yes" which, however, provides no reason for an answer on a highly controversial subject.

TRIAL EXAMINER: Very well. All of the answer to the question other than "Yes" is stricken.

By MR. SPARKS:

Q. Can an outstanding issue of bonds be redeemed and onerous requirements of an existing debt contract avoided without the payment of call premiums? A. No.